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BusinessWeek

THE LOST GENERATION

The job crisis is hitting young people especially hard—imperiling their future and the economy

BY PETER COY



PLUS:
WHAT'S SLOWING INDIA'S GROWTH


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(INDIA COVER AND ABOVE) MATT MAHURIN; (LOST GENERATION COVER) RODRIGO CORRAL

IN DEPTH

THE LOST GENERATION AND THE ECONOMY

032 | The wave of unemployment ravaging the globe is doing the most damage to young people. The risk is that they'll be scarred for life—their earning potential permanently stunted. And that could be bad for entire economies, as well. | BW |

WHAT'S SLOWING GROWTH IN INDIA

038 | The subcontinent's industrial revolution has hit a roadblock: Indian farmers are standing in the way of $98 billion worth of projects, ranging from steel mills to airport expansions. It doesn't look like either side of the conflict is about to back down. | BW |

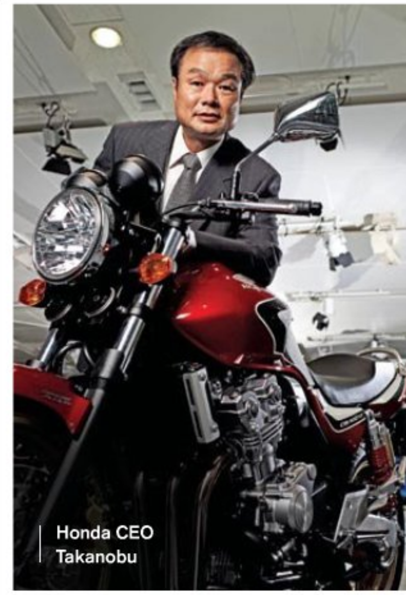
BETTING BIG ON A BOOM IN NATURAL GAS

046 | Prices for this cleaner form of energy have dropped as vast new reserves hold out the promise of a reliable supply of gas in the years ahead. That prospect has a wide range of coal- and oil-powered businesses making the switch. | BW |



THE U.S. CHAMBER OF CONFLICT

Now that Steve Jobs has left the business group—Apple is the fourth major company to quit over the Chamber's opposition to climate legislation—the U.S. Chamber, led by Tom Donohue, may be losing credibility and clout. BW | PAGE 022



Honda CEO Takanobu

WHY HONDA ISN'T HURTING

While Nissan and Toyota bleed billions, the maker of fuel-sipping cars—and more motorcycles than anyone else—is safely in the black, thanks to its nimble corporate culture. BW | PAGE 057

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Jack and Suzy Welch are off while Jack recovers from a back infection.

(L TO R) PHILIP BURKE; MAKOTO ISHIDA


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THE BUSINESS WEEK

EDITED BY HARRY MAURER & CRISTINA LINDBLAD



Cutting hair in California: The service sector ticked up for the first time in a year

SANDY HUFFAKER/CORBIS

ECONOMICS & POLICY

SERVICES SHOW SOME LIFE

Damn the mixed signals—full speed ahead! That's apparently what investors concluded on Oct. 5-7 as they piled back into stocks and pushed up the **S&P 500** by 3.2%. The job news continued to be grim, with the **Labor Dept.** reporting on Oct. 2 that payrolls fell by a worse-than-expected 263,000 in September and unemployment rose to 9.8%. But the **Institute for Supply Management** said on Oct. 5 that in September its nonmanufacturing index edged above 50, to 50.9—a sign that service industries are expanding after 11 straight months of contraction. The ISM manufacturing index came in at 52.6, its second consecutive month of growth. And consumer spending grew by an inflation-adjusted 0.9% in August, said the **Bureau of Economic Analysis,** though most of that was due to the cash-for-clunkers program, which ended on Aug. 24, so spending could fade in September. Inflation fears, meanwhile, continue to propel gold bugs into fits of ecstasy. The lustrous metal closed at an all-time nominal high of $1,044.20 an ounce on Oct. 7 as the dollar's seven-month slide resumed.

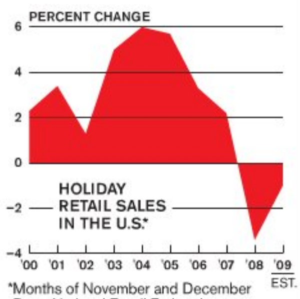
CAVEAT ENDORSER

If you get paid to review products online, you'll have to mind your p's and q's a bit more closely. In its first update of endorsement guidelines in 29 years, the **Federal Trade Commission** said on Oct. 5 that bloggers and other online mavens who get cash or freebies to evaluate goods are essentially endorsers—and should disclose any "material connection" to the seller. The rules also require ads to reflect "the results that consumers can generally expect," ending a loophole that allowed marketers to cite glowing but atypical results. Commercials must disclose links between advertisers and

research cited in an ad. The agency warned that celebrities and other endorsers can find themselves on the hook for "false or unsubstantiated" claims, as well as failures to disclose pecuniary ties.

BAH HUMBUG!

Retail sales are set to fall again this holiday season



*Months of November and December
Data: National Retail Federation

THE PAY CZAR TAKES AIM

Top brass at firms awash in bailout money may have to start pinching pennies. According to *The Wall Street Journal* on Oct. 6, the Obama Administration's "pay czar," **Kenneth Feinberg,** will crimp their take-home pay by requiring them to transfer around 50% of their salary to stock they can't touch for several years. By mid-October, Feinberg may be prepared to announce his compensation plan for companies that received the most bailout money—including **American International Group, Bank of America,** and **General Motors.** The Administration claims the move isn't a punishment but rather an incentive for managers to make smarter decisions, given that their pay will be tied to stock performance. The goal is to end shortsighted moves that can garner robust bonuses but lay the groundwork for another disaster.

RIO GRABS THE GOLD

Quick, pick the venue with the most sex appeal: **Chicago, Madrid, Rio de Janeiro,** or **Tokyo?** Not much of a contest there. Unfurling its theme of "Live your Passion," Rio on Oct. 2 was selected to host the 2016 **Olympics. President Luiz Inácio Lula da Silva,** joined by soccer legend **Pelé,** cried in Copenhagen after making a fervent pitch for the Summer Games to be held for the first time in South America. On Copacabana beach, tens of thousands of Brazilians partied in string bikinis and body paint. Now the not-so-sexy work begins: building infrastructure that functions in a city more focused on play. City fathers promised to pour $14.4 billion into stadiums, highways, security, and other improvements. **U.S. President Barack Obama,** who recently called Lula "the most popular politician on earth," was lambasted in some quarters for expending his own star power in support of Chicago's doomed bid.

| BW | PAGE 061 "Brazil's Olympic Jump"



Feinberg: New rules on bank pay

JOSHUA ROBERTS/BLOOMBERG NEWS

HILTON UNDER SCRUTINY

Was **Hilton Worldwide** hospitable to purloined papers? *The Wall Street Journal* said

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PCWorld

Sprint tested as the most reliable 3G network overall among U.S. carriers in a recent 13-city 3G performance test conducted by *PC World*.

Coverage not available everywhere. Data plan required. Connectivity dependent upon capability. The 3G Sprint Mobile Broadband Network reaches over 253 million people. Offer not available in all markets/retail locations or for all devices/networks. Other restrictions apply. See store or sprint.com for details. *PC World's* tests included 13 major cities with more than 20 tests per city from all regions of the country for each provider's 3G service. Testing was one minute in duration, and network performance can be highly variable from neighborhood to neighborhood. ©2009 Sprint. Sprint and the logo are trademarks of Sprint. Other marks are the property of their respective owners.

on Oct. 7 that a federal grand jury in New York is considering criminal charges against the company and several of its former executives in what could turn out to be a massive case of corporate espionage. In April rival **Starwood Hotels & Resorts** sued Hilton, accusing two ex-Starwood managers of stealing thousands of pages of documents detailing its new hotel concepts. Hilton has fired nearly a dozen staffers in connection with the case. A company spokesperson says it is cooperating fully with investigators.

STRATEGY

COMCAST'S PEACOCK?

We won't sell it. We wouldn't dream of selling it. Well, O.K., maybe we'll sell it. **General Electric,** which has insisted for years that it wouldn't part with its **NBC Universal** studio and TV unit, is negotiating to give up control in a complex deal suggested by cable giant Comcast. Under the proposal, Comcast would own a 51% stake in a newly created private powerhouse that would include its **E! Entertainment** channel and other assets as well as GE's media properties. Comcast would also give around $6 billion to General Electric, which would then pay French telecom giant **Vivendi** roughly the same amount for its 20% holding in NBC Universal.



Football on NBC: Comcast is negotiating to buy the network from GE

| BW | PAGE 028 "A Touchdown for Comcast?"

EXXON FILLS 'ER UP

Sure, $4 billion amounts to a drop in the barrel for **Exxon Mobil,** yet its purchase of a 23% stake in an offshore Ghanaian field is its first major acquisition since Exxon snapped up Mobil for $82 billion way back in 1998. What moved the oil behemoth to buy in? The field, named **Jubilee,** lies in a promising, entirely new oil region, and Exxon must begin to pump up its reserve base after years of tapping existing properties. The deal demonstrates yet again the company's tradition of swooping in to snatch up

IDEAS FROM THE DESERTS OF IRAQ TO THE MBA CLASSROOM

U.S. B-schools are looking for a few good men—and women. Dozens of MBA programs have signed up for the **Yellow Ribbon** program, an initiative created by the **Post-9/11 Veterans Educational Assistance Act of 2008,** reports *BusinessWeek*'s Alison Damast. Under Yellow Ribbon, which took effect this fall, Washington commits to pay vets a base level of tuition, plus match any financial aid offered by participating schools—and throw in stipends for housing, books, and supplies.

B-schools in particular are hoping the new program will help them draw more veterans, who by some estimates now make up a scant 4% of the MBA population. Among the schools that have signed up are marquee names such as **Columbia, Harvard, Stanford,** and the **University of Pennsylvania's Wharton. Dartmouth's Tuck School of Business** is committing $19,233 per student, which along with the federal money covers all of the annual $47,835 tuition.

The **Veterans Benefits Administration** is still compiling data from all colleges and grad schools on how many veterans have enrolled. But the agency is anticipating a groundswell of interest and forecasts that some 440,000 vets will take advantage of the revamped GI Bill.

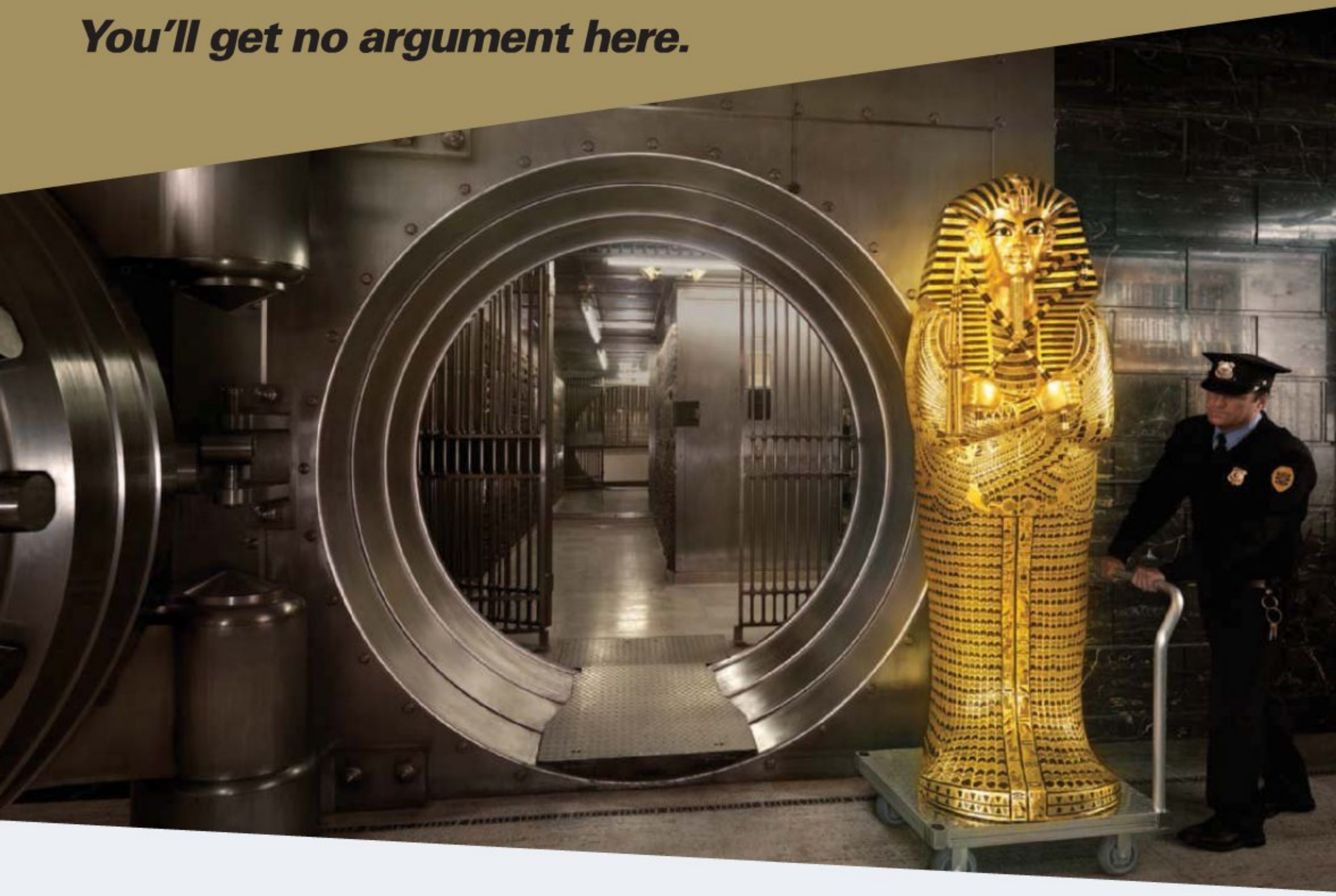
"Why Veterans Are Saluting Business Schools" businessweek.com/magazine



FDR signs the first GI Bill in June 1944

(TOP) ZADE ROSENTHAL/NBCU PHOTO BANK/AP PHOTO; (BOTTOM) BETTMANN/CORBIS

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Two ex-Ford officials put in a bid for Volvo

oil-patch goodies found by risk-taking wildcatters.

LEADERSHIP

CHRYSLER CLEANS HOUSE

That didn't take long. Notoriously tough Chrysler **CEO Sergio Marchionne** wielded the broom on Oct. 5, sweeping out two executives—**Dodge President Michael Accavitti** and **Chrysler brand President Peter Fong**—just three months after promoting both. Marchionne was known for shaking up the C-suite after he took over **Fiat** in 2004. Meanwhile, former **Ford** executive **Shamel Rushwin** and past Ford board member **Michael Dingman** put in a bid for the company's Volvo unit. China's **Geely Holding Group** is the other bidder.

BOFA'S SEARCH

Bank of America's mostly new directors may barely know each other, but their first task will be a doozy: Picking a new CEO. **Ken Lewis,** who dropped a bombshell on Sept. 30 by saying he'll step down by yearend, may have to be replaced before that if his legal woes worsen. The two internal contenders are consumer banking head **Brian Moynihan** and chief risk officer **Greg Curl,** but the board may opt for a transitional chief executive to give young candidates such as Moynihan more time to ripen. If they go that route, the contenders include **ex-CFO Jim Hance** and **former Merrill Lynch President Greg Fleming.**

FINANCE

PURSUING LEHMAN FUNDS

The slow unwinding of the **Lehman Brothers** collapse drags on. Frustrated with the courts, some Lehman hedge fund clients who have had accounts worth nearly $9 billion tied up in London bankruptcy proceedings for more than a year are trying to find a way out on their own. The funds and administrators from **PricewaterhouseCoopers** said on Oct. 6 that they are seeking the consent of a substantial majority of clients to go ahead with a plan to distribute the available money without court approval. A British judge ruled on Aug. 21 that he did not have jurisdiction to certify such a scheme. The administrators are appealing that decision but don't want to wait patiently for the outcome.

TECHNOLOGY

BROCADE ON THE BLOCK

Techdom has seen plenty of M&A lately, though nothing like the frenzy many experts expect as **Cisco, Hewlett-Packard, IBM, Intel, Microsoft,** and **Oracle** strive to become one-stop providers of cloud computing services. Get set for more: On Oct. 6 word spread that **Brocade Communications** was seeking buyers. Potential suitors for the networking company, which may fetch $4 billion-plus, include HP and **Juniper Networks.** If Brocade does sell, other giants could be pressured to buy more large, second-tier tech outfits.

E-CARS FROM TURKEY

At this year's Frankfurt auto show, electric cars accounted for much of the electricity—and one of the models was a plug-in version of **Renault's Fluence,** which will be manufactured in Turkey beginning in 2011. Ankara hopes Renault's investment will lure other automakers to build eco-friendly cars in the country, reports the Nov. 4 edition of *BusinessWeek Turkey*, helping boost overall auto production from its current level of 1.1 million vehicles per year. But that may prove a hard sell, given that there is no domestic market yet for these pricey machines. Nor are there plans afoot to develop the infrastructure needed to support plug-in vehicles.



24.3%

Average decline in the value of 401(k) accounts in 2008

37%

Drop in the S&P 500 index in 2008

Data: Investment Company Institute

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WHY THE EARNINGS FORECAST IS UPBEAT

With productivity skyrocketing and labor costs plunging, profits will post strong growth in coming quarters now that demand is beginning to turn up

It's earnings season, and as companies roll out their third-quarter reports, investors are sure to take a long, hard look at the results. Profits in the first and second quarters, while down from the previous year, managed to beat expectations, helping the Standard & Poor's 500-stock index to ascend more than 50% from its low point on Mar. 9. Amid ongoing worries about the strength and sustainability of the recovery, which were heightened by the weaker-than-expected jobs report for September, investors want to see if earnings will validate this year's big market run-up.

$75.61

Analysts' projection for 2010 earnings per share for the S&P 500 companies, vs. an expected $59.95 in 2009

Data: Thomson Reuters

The signs look good, and last month's employment data are part of the reason. Through the third quarter, businesses continued to slash labor costs at rates not usually seen even in past severe recessions. In fact, for the past six quarters, companies have cut employees' overall hours worked by far more than they have pared output. The result: a striking 2.8% annual rate of growth in productivity, a rare pace during a recession. Productivity gains averaged only 0.8% annually during the previous nine downturns.

Of course, these are not long-run productivity gains: Businesses cannot slash and burn their way to prosperity. However, they can soften the recession's blow to their bottom lines and put themselves in a position to reap the benefits of the recovery as demand picks up. That's what's happening right now, and that's why third-quarter earnings are likely once again to surprise on the upside.

The September payroll numbers showed that overall hours worked in the third quarter fell at a 3% annual rate from the second quarter. If economists are correct in expecting about 3% growth in real gross domestic product for the quarter, then productivity may well post its second consecutive quarterly advance of about 6%. That would mean unit labor costs, or pay adjusted for productivity, are set to plunge for the third quarter in a row. In fact, unit labor costs, which are a key factor in determining profit margins, appear to have posted the largest three-quarter decline since quarterly data began in 1947 (chart).

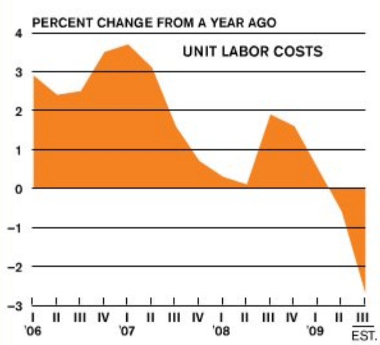
As company reports begin to trickle in, analysts expect third-quarter earnings per share for the S&P 500 companies to decline 24.8% from a year ago, smaller than the losses in each of the three previous quarters, according to the latest survey by Thomson Reuters. Eight of the 10 major sectors are expected to post drops, with only the financial and consumer discretionary categories showing increases.

However, as in previous quarters, investors will be focused on how companies perform relative to expectations. One key benchmark will be the number of firms that beat current estimates. In the second quarter, 73% of the S&P 500 performed better than expected, a percentage reached in only one other quarter since Thomson Reuters has kept records. Third-quarter reports appear to be on a similar track. So far, there have been 64 negative pre-announcements, or companies saying they will miss their targets, and 42 positive alerts. That ratio of 1.5 is well below the historical average of 2.1. In fact, that low reading matches the ratio at this stage of the stronger-than-expected second quarter.

The earnings punch from recent productivity gains should be especially evident in the Commerce Dept.'s economy-wide roundup of corporate profits, due on Nov. 24. These numbers cover thousands of firms and are seasonally adjusted to allow tracking from quarter to quarter. They show that the upturn in earnings actually began in the first quarter. Profits in both the first and second quarters rose from the previous quarter, even though sales fell in both periods. What is different in the third quarter is that overall demand is now rising amid an ever more favorable cost structure.

As last month's job data showed, the downside of companies' aggressive commitment to productivity and profits will be very slow improvement in the job markets. However, as demand strengthens, solid earnings will help to drive corporate expansion, the foundation of a sustainable recovery. | BW |

AGGRESSIVE COST CONTROL IS BUOYING PROFITS



Data: Labor Dept., IHS Global Insight, *BusinessWeek*

BRAD TRENT; CHART BY DAVID FOSTER

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NUMBERS

HOPEFUL SIGNS? NOT ALL INVESTORS THINK SO

By Tara Kalwarski/Charts by David Foster

The U.S. stock market posted sterling gains in the third quarter, and consumers' economic expectations are the highest since the downturn began. But some investors are betting on a market pullback.

Consumer outlook: Expectations for the economy are up.



*Based on expectations about business and employment conditions and income six months from now
Data: Conference Board

Big bounce: The past half year is among the best ever.

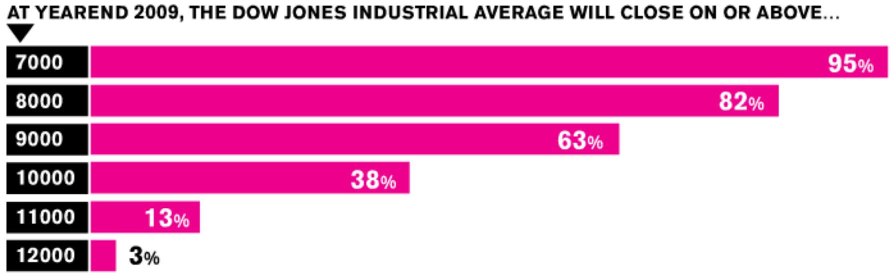
BEST SHOWINGS FOR THE STANDARD & POOR'S 500-STOCK INDEX FOR THE SIX MONTHS ENDED...

Q3 1933	66.2%
Q2 1933	57.7%
Q4 1932	56.2%
Q3 1938	44.0%
Q2 1975	38.8%
Q3 1935	37.2%
Q3 2009	32.5%

Data: Bloomberg

Down on the Dow: Only 38% of investors betting in an online prediction market expect the Dow to end the year above 10,000.

AT YEAREND 2009, THE DOW JONES INDUSTRIAL AVERAGE WILL CLOSE ON OR ABOVE...

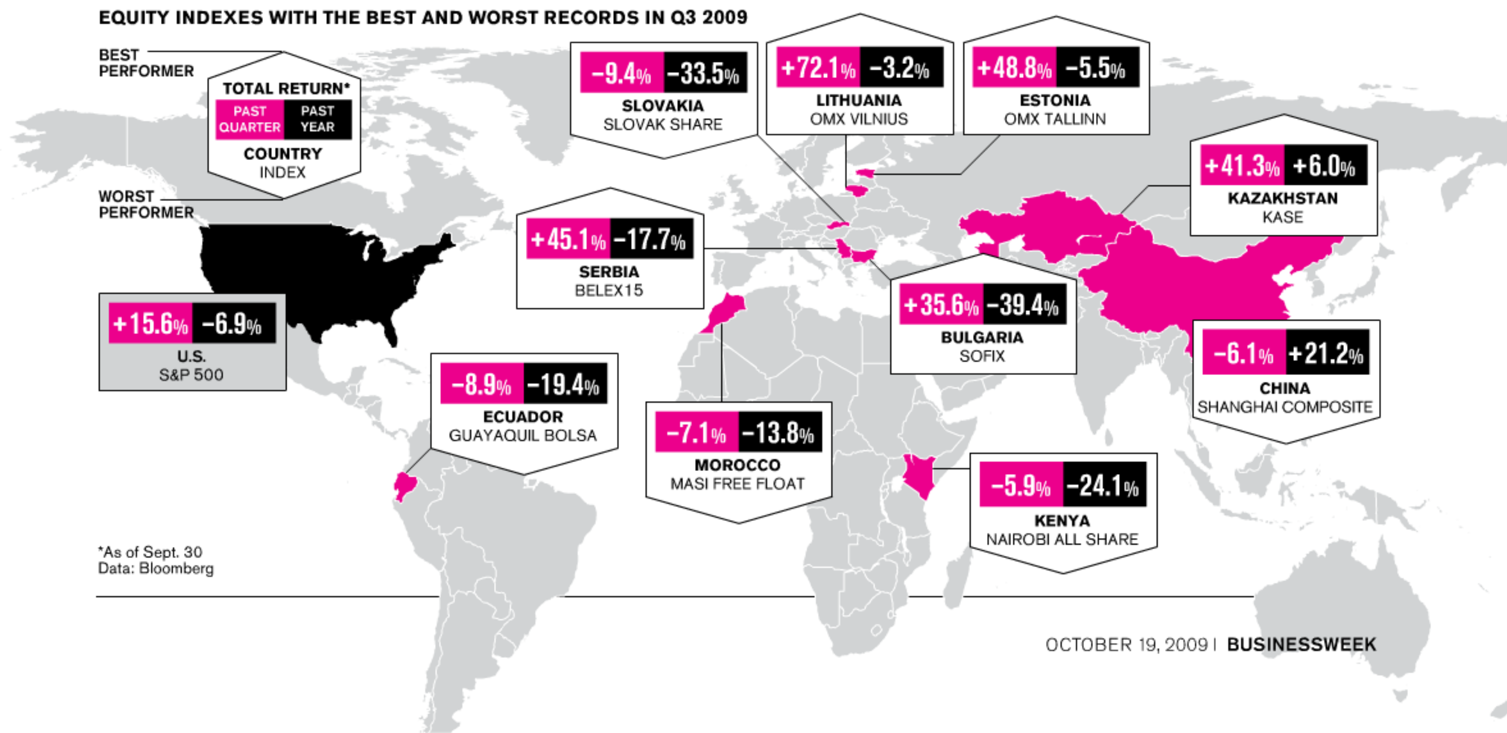


Data: Intrade Prediction Market
*As of Oct. 2

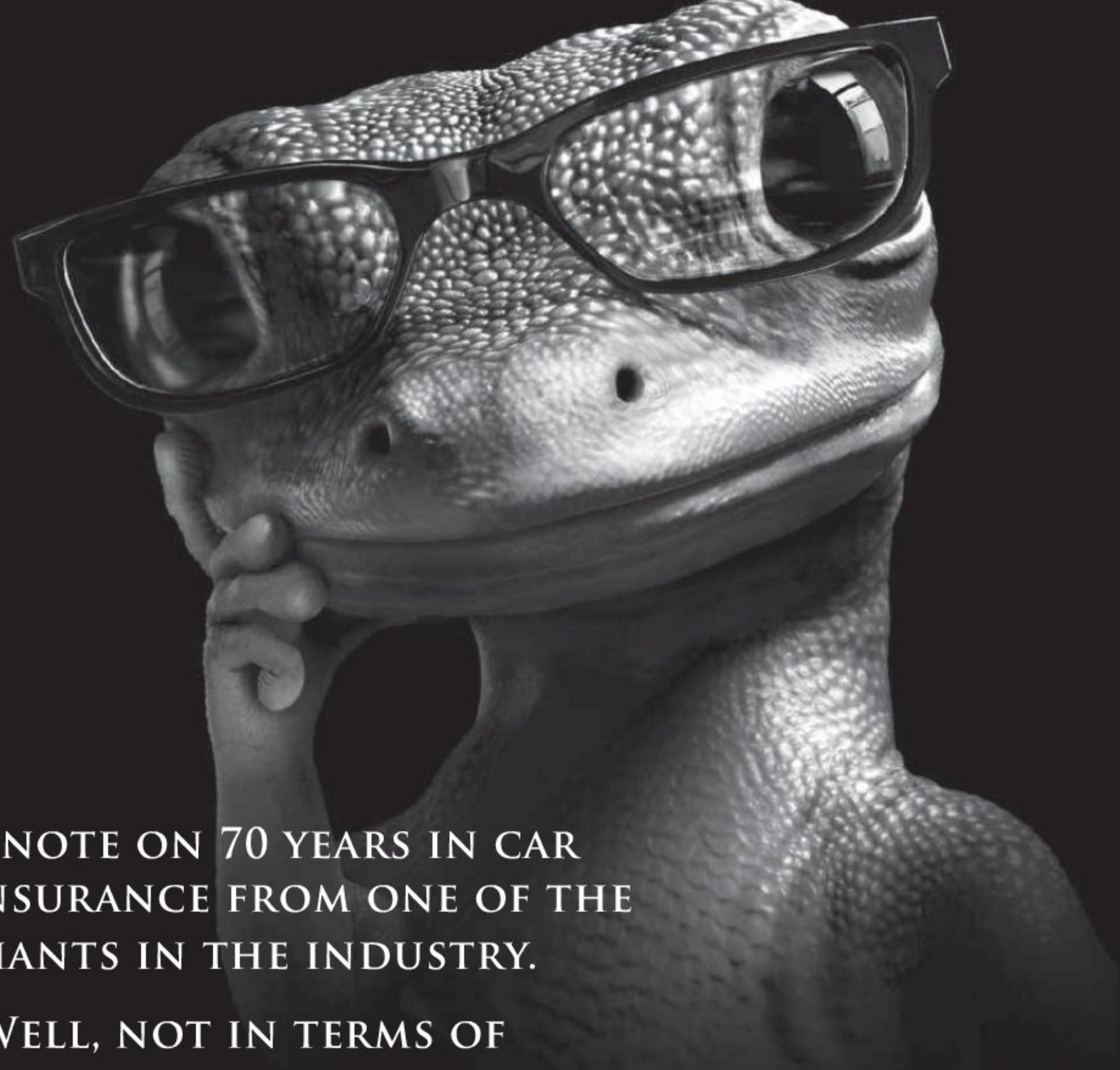
GLOBAL GLOOM

Most of the third quarter's best-performing stock indexes are still down on a year-over-year basis.

EQUITY INDEXES WITH THE BEST AND WORST RECORDS IN Q3 2009



*As of Sept. 30
Data: Bloomberg



A NOTE ON 70 YEARS IN CAR INSURANCE FROM ONE OF THE GIANTS IN THE INDUSTRY.

(WELL, NOT IN TERMS OF HEIGHT, OF COURSE.)

What the Gecko lacks in stature he certainly makes up for in ability. In fact, under the ownership of Warren Buffett's Berkshire Hathaway Inc., he's helped GEICO rise to become the nation's third-largest car insurance company. Of course, the fact that GEICO has been helping people save money on car insurance for over 70 years hasn't hurt either. And when it comes to financial security, GEICO is consistently ranked "excellent" or better by independent experts. But even though it's not common practice to have geckos in the highest levels of business, this one inspired three million drivers to switch to GEICO last year (and never missed a day of work). Perhaps proving that you can be both big and small at the same time.

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FACETIME | MARIA BARTIROMO





(TOP) BRAD TRENT; (BOTTOM) HERMANN BREDEHORST/POLARIS

SIEMENS CEO LÖSCHER LOOKS TO THE FUTURE

In late September, Siemens issued an ultimatum to former board members, including ex-CEOs Klaus Kleinfeld and Heinrich von Pierer: Reimburse the company for some of the money it has expended to settle a massive corporate bribery scandal or face legal action. According to the *Financial Times*, Siemens wants Kleinfeld, now chief executive of Alcoa, to pay more than $2.9 million; it is seeking about three times that from von Pierer. Siemens claims that its former chieftains failed to stop widespread bribery, first revealed in 2006. The scandal has become a long-running embarrassment for a company *The Guardian* called "a symbol of German engineering excellence and corporate probity." In 2007, current Siemens CEO Peter Löscher, a former top executive at Merck, was brought in to clean up the mess, which has cost the company billions in fines and legal fees. I talked with him about what is perhaps the final chapter of the saga and about how he sees the global recovery shaping up from his vantage point atop a major multinational.

MARIA BARTIROMO
Siemens has threatened legal action against former executives if they don't reimburse the company for some costs related to the bribery scandal. What exactly are you looking to accomplish?

PETER LÖSCHER
This case is currently being [negotiated] between the supervisory board of Siemens and the former executive board members. Clearly the company has indicated that it wants to settle under certain conditions. Now it's up to the two parties to find out if they're willing to settle.

Have you gotten any indications from the former executives, Kleinfeld and von Pierer, if they are going to settle?
I don't want to go into details because this is really a supervisory board matter. The company, from a management perspective, has moved beyond these issues.

Do you think they could face legal action?
The supervisory board, at its last meeting, set a time limit of mid-November [to reach an agreement]. The company is prepared to take legal action in this unfortunate situation, if necessary. My understanding is that everybody's now focused on how to settle the case.

Yours is a business that provides an overview of the global economy. How would you characterize the economy right now?
The global economy has certainly bottomed, and we have some encouraging signs. We see a distinct growth pattern around the world; very solid growth in China, India, Brazil, and in parts of the Middle East.

What are strongest areas, and is China's recovery for real?
China was extremely effective in how it implemented its stimulus program. We see very solid growth in infrastructure development—energy, energy transmission, and the whole rail modernization program. We also see growth in the Middle East, in countries like Abu Dhabi and Qatar.



Kleinfeld in April 2007, the day after announcing he would leave Siemens

MICHAELA REHLE/REUTERS/CORBIS

How does Europe look to you?
There are difficult market environments in the UK and Spain. Very difficult environment in the eastern bloc of Europe, still impacted by limited credit facilities. I think we are seeing the first positive signs coming out of Germany.

Will the victory by German Chancellor Angela Merkel's center-right alliance have a significant impact on the recovery in Germany and, by extension, Europe?
I believe the new government will quickly focus on overcoming the economic crisis and then on how to approach the climate change agenda together with its core international partners.

> **The [Merkel] government will quickly focus on ... the climate change agenda with its core international partners**

Let me ask you about protectionism. Have you seen a resurgence of nationalistic behavior within the EU as a result of the recession?
We don't see a resurgence of protectionist measures. But we have to be very vigilant. At the end of the day, [protectionism] affects all companies in really negative ways. Protectionism and trade wars provoke countermeasures, which endanger exports and therefore jobs.

Do you think that inventories have been depleted enough to where companies will be forced to start reordering?
Yes. In some areas of our industrial businesses we actually see a restocking happening.

And as far as commodities prices, what do you expect? We see oil, gold, copper, all sorts of commodities on the rise. Does this concern you?
No, not at all. I think it's probably a sign also that the worst is behind us.

Have you used the recession to refine your strategy?
Yes, we have reshaped Siemens in record time. And very much from a strategic perspective. We are focused on our core growth markets. Of course the U.S. is very important to us, so we will continue to invest there, where in the last six years alone we have invested more than $26 billion. We have more than 70,000 people and 800 locations in 50 states. We continue to invest alongside the Obama stimulus package. There's a huge, huge shift toward positioning Siemens as the green infrastructure company. We have the broadest and deepest green portfolio of any company in the world. | BW |

Maria Bartiromo is the anchor of CNBC's Closing Bell and writes the blog, Maria Bartiromo's Investor Agenda, at http://investoragenda.cnbc.com



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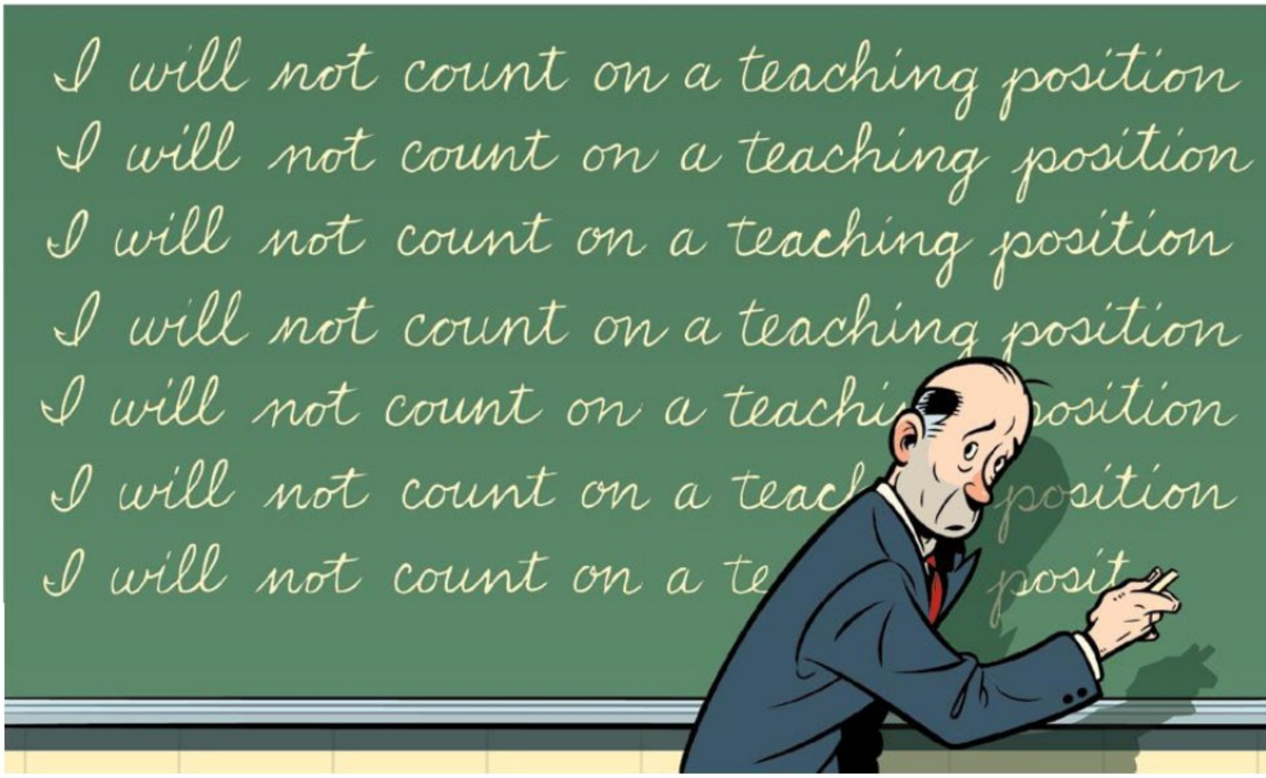


ILLUSTRATION BY MARK MATCHO

THE RECESSION GOES TO SCHOOL

For decades, teaching has been a secure profession—combining service with a steady living in good times and bad.

Not in this recession. The gloomy federal jobs report issued by the Labor Dept. on Oct. 2 showed a record decline in education jobs in September from the same time last year.

The drop in public and private employment for elementary, secondary, and technical schools, as well as higher education, was 0.9%, or 121,000 positions. That's the biggest slip since such record-keeping began in the 1950s. And for the first time, the decline comes as enrollments are rising. "You haven't had state and local governments this stressed since the Great Depression," said Dean Baker, co-director of the Center for Economic & Policy Research, a Washington think tank.

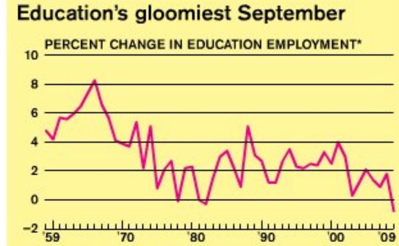
The penetration of layoffs into one of the most recession-resistant kernels of the economy shows how pernicious the downturn remains. Take a look at history: Just three previous Septembers—in 1978, 1981, and 1982—had year-over-year education job drops (chart).

Each of those dips was smaller than the current decline and came as school enrollment shrank. (While enrollment numbers for the current year aren't yet available, the latest report from the Education Dept. projects the number of students—those in elementary school through college—will rise this year.)

In budget-strapped Los Angeles Unified School District, 2,100 teachers, counselors, and others were let go this school year as average class size rose to 24 students from 21. "It's only going to get worse next year," predicts Gregg Solkovits, vice-president for secondary education for the United Teachers of Los Angeles.

—Michael Mandel and Steve LeVine

Education's gloomiest September



*Year-over-year for September; includes state, local, and private-sector educational employment
Data: Bureau of Labor Statistics

THE MOXIE TO TAKE ON MATTEL—AGAIN

A year after a court gave Mattel the rights to MGA Entertainment's Bratz dolls in a dispute over the line's origins, MGA has launched two new dolls, both aimed at Mattel's business. Fashion-focused Moxie Girlz are targeting Barbie. Best Friends Club is a line of larger dolls—each with a backstory and a journal—meant to take on the historically themed American Girl. "Mattel thought it would kill MGA and have a doll monopoly," says MGA CEO Isaac Larian, who is appealing last year's jury verdict. "MGA came back with not one, but two." Both are designed with the weak economy in mind, Larian says. Whereas Bratz dolls went to pretend discos in $69.99 plastic limos, Moxie Girlz ($17.99) ride in a $29 hybrid. Best Friends Club dolls sell for $39, compared with $95 for Mattel's American Girl. To promote the dolls, Larian plans to run ads in magazines such as *Parenting* that declare: "Your daughter's best friend shouldn't cost a fortune." Oh, and he seems to have picked up a thing or two from the intellectual property skirmish with his rival. Visitors to MGA's offices are now asked to sign an agreement saying they'll consult with MGA before discussing any trade secrets they may come across. "I borrowed a couple of paragraphs from Mattel," Larian says with a grin. *–Christopher Palmeri*

MGA's new Moxie Girlz can be paired with $29 hybrid cars





"Peggy Sue," the first U.K. Greyhound

BRITAIN GOES GREYHOUND

Greyhound is crossing the Atlantic. On Sept. 14, Greyhound UK began offering service between London and two coastal cities, Portsmouth and Southampton. To capitalize on the company's American roots, buses have been named after women from classic U.S. songs—there's a Proud Mary and a Barbara Ann. "Even in Britain, everyone recognizes the brand," says Alex Warner, Greyhound UK's managing director.

With cash-strapped British passengers trading down from rail travel and local bus rivals taking longer to cover the same routes, Greyhound is competing by offering non-stop service and amenities—Wi-Fi, power outlets, and complimentary newspapers.

$1.60

Greyhound UK's lowest one-way price for the two-hour journey between London and Britain's south coast.

The 11-bus fleet is modeled on Boltbus, Greyhound's successful discount service on the East Coast of the U.S. One-way prices start at a pound ($1.60) for the two-hour journeys Greyhound now offers.

Warner says the British adventure is set to break even by 2010. Routes to five other British destinations are planned for next year, mostly to cities no more than three hours from London with large student populations or tourist attractions. *–Mark Scott in London*

(TOP, RIGHT) PHOTOGRAPH BY OLI SCARFF/GETTY IMAGES

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WHO SPEAKS FOR BUSINESS?

The U.S. Chamber's fight against a climate bill is costing it credibility, clout—and members

By Jane Sasseen

There aren't many who would willingly take on Apple icon Steve Jobs—and lecture him on technology. But Thomas J. Donohue, the combative head of the U.S. Chamber of Commerce, isn't one to step away from a fight.

So on Oct. 6, a day after Apple became the fifth—and most prominent—company to resign or reduce its role at the Chamber because of its aggressive opposition to climate change legislation, Donohue fired back. "It is unfortunate that your company didn't take the time to understand the Chamber's position on climate and forfeited the opportunity to advance a 21st century approach," he wrote to Jobs. He stressed the Chamber's belief that business can spur much of the technology to reduce greenhouse gases, much as the private sector has "developed the innovations that we now take for granted, from the personal computer to the medicines that keep us healthy."

Donohue is renowned for his bulldog style. Now he and his colleagues find themselves embroiled in a fight over climate change that raises questions about how broadly they speak for business—and whether the Chamber, allied with the Republican Party for the last decade, can retain its influence in a heavily Democratic Washington.

$100 MILLION WAR CHEST

The Chamber has moved sharply to oppose much of the legislation and many of the regulations and policies streaming out of the Obama Administration and the Democratic Congress on health care, labor issues, and finance. In a move some see as little short of a declaration of war on the White House, Donohue has been crisscrossing the country to raise $100 million to launch the "Campaign for Free Enterprise." It is intended to promote open markets and fight a rise in regulations and tax hikes that he argues will undermine job creation and the economy. "We are certainly not alone," says Donohue, adding that the Chamber's controversial policy choices reflect his members' views: "This is not me ... This is not my staff. We are delivering on the issues that concern the business community."

The less partisan Business Roundtable is developing a strong working relationship with the White House

Many well-placed Democrats believe that hard-nosed attitude is starting to cost the Chamber credibility—on energy and beyond. "The more they get out in opposition on core issues to the Democrats, the more they will continue to alienate them," says a top aide to a key Democrat in the Senate. "The Chamber's best shot is to influence moderate Democrats, but the more unrealistic they get, the more they will leave the moderates wondering why they should work with them." As proof of the Chamber's flawed approach, Democrats point to its recent leading role in what many saw as an over-the-top attack on the Administration's plans for an agency to protect consumers from predatory lenders. Even moderate Democrats who are often supportive of the Chamber took note. "It's unfor-



ILLUSTRATION BY PHILIP BURKE



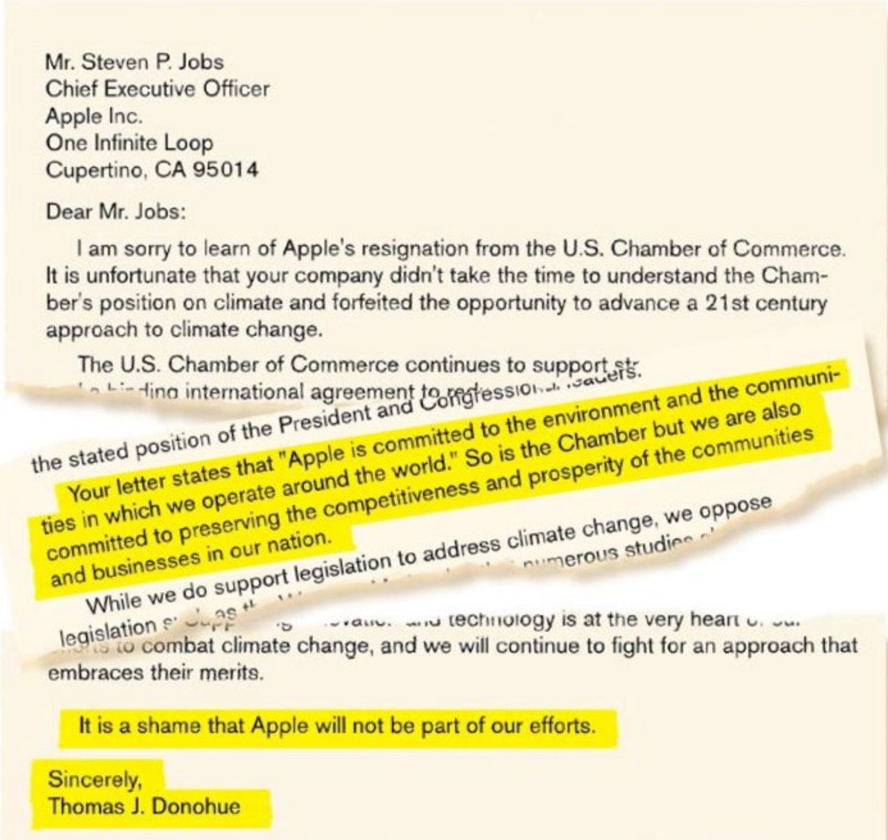
tunate that some business groups are allowing misleading information to confuse the debate," says one influential representative in financial matters, referring to claims by the Chamber and others that many small businesses would be covered by the proposal. "We should be debating the real issues."

The Administration, meanwhile, is going out of its way to foster ties with CEOs and business leaders on its own, rather than rely on the Chamber. "I'd rather talk to [Cisco boss] John Chambers than to the Chamber," says Valerie Jarrett, the Presidential adviser responsible for outreach to the business community. "I don't stop listening to the Chamber, but [the resignations] do make me question whether they have the pulse of their membership." Adds Hilary Rosen, managing partner of the D.C. office of communications strategy firm Brunswick Group and a White House confidant: "Most business leaders we speak to are looking for solutions. The Chamber's posture has become a barrier."

The White House appears to be turning more to the Business Roundtable, a group of over 160 CEOs, for feedback and input on its policies. John Castellani, the Roundtable's president, says its members have met frequently with White House staff in recent months. The group's leaders, such as Ivan G. Seidenberg of Verizon Communications and Andrew N. Liveris of Dow Chemical, have featured prominently on the list of CEOs invited to dine with the President or his top aides.

U.S. Chamber Chief Donohue (center) says CEOs are holding back

The Roundtable is seen as having a more pragmatic take on the business community's agenda. "We strive to be politically relevant, but not partisan," says Castellani. Much of its work is



Mr. Steven P. Jobs
Chief Executive Officer
Apple Inc.
One Infinite Loop
Cupertino, CA 95014

Dear Mr. Jobs:

I am sorry to learn of Apple's resignation from the U.S. Chamber of Commerce. It is unfortunate that your company didn't take the time to understand the Chamber's position on climate and forfeited the opportunity to advance a 21st century approach to climate change.

The U.S. Chamber of Commerce continues to support st...
...ding international agreement to...
the stated position of the President and Congressional leaders.

Your letter states that "Apple is committed to the environment and the communities in which we operate around the world." So is the Chamber but we are also committed to preserving the competitiveness and prosperity of the communities and businesses in our nation.

While we do support legislation to address climate change, we oppose ... numerous studies ...
legislation ... technology is at the very heart ...
... to combat climate change, and we will continue to fight for an approach that embraces their merits.

It is a shame that Apple will not be part of our efforts.

Sincerely,
Thomas J. Donohue

chief of staff to PG&E's chief executive. "The difference on this issue—where we were and where the Chamber wanted to go—was just too significant."

That rebellion is now spreading from utilities to consumer companies that are burnishing their green credentials. On Sept. 30, Nike announced that it would resign from the Chamber's board, although it will remain in the group and continue to debate climate change from within. Not so Apple, where CEO Jobs recently stepped up efforts to reduce its own emissions. On Oct. 5 the maker of the iPod withdrew from the Chamber. In a letter to Donohue, Apple chastised the Chamber, saying: "It is frustrating to find the Chamber at odds with us in this effort."

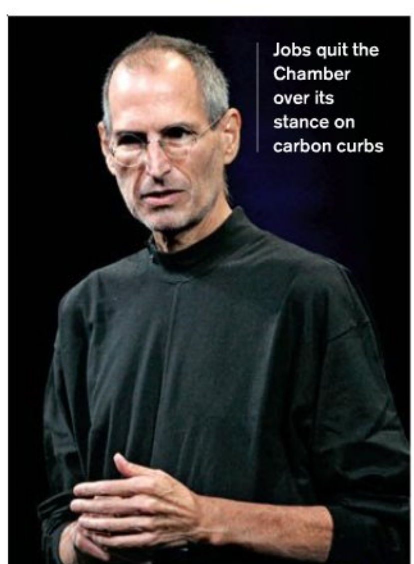
Donohue minimizes the importance of the defections. While he says the group would

data driven. On climate change, the Roundtable neither opposes nor favors a tax or a cap-and-trade system as the best way to put a price on carbon emissions. Instead it has provided policymakers with extensive data on how different companies and markets would react at different price levels.

Donohue maintains many chief executives hold back on what they really think when dealing with the Administration. "We see CEOs act all friendly to get a seat at the table," he says. "Then they call us up and say: 'You better fix this.' " He plays the bad cop, the guy who has to tell it straight.

That dynamic has been driving the fight over climate change. The Chamber vehemently opposes legislation now before Congress as well as moves by the Environmental Protection Agency to regulate harmful carbon emissions. In late August a top Chamber official even called for a public hearing, similar to the Scopes Monkey Trial, to rule on the evidence of human responsibility for global warming.

The Chamber has since repudiated the remarks, which referred to the 1925 trial that pitted religion against evolution. Donohue says the Chamber doesn't dispute the science of global warming, but it wants more debate on how the U.S. regulates it. Still, the damage was done: Utilities PG&E, Exelon, and PNM Resources, all of which back the congressional legislation, quit. "We came to the conclusion that the legislation they were looking for was not the legislation that would address carbon," says Shawn Cooper,



Jobs quit the Chamber over its stance on carbon curbs

ROBERT GALBRAITH/REUTERS/CORBIS

support strong curbs if they were combined with an effective international pact, it doesn't back the current legislation because it would hurt U.S. competitiveness. Those who have quit, he implies, either will benefit from the legislation or won't be harmed. What the opposition suggests "is that we are having an effect," he says. "We are amongst those who have raised serious questions about the content of the legislation."

Plenty of companies are sticking with the Chamber. Dow is in the Chamber as well as the Roundtable, but supports the current climate legislation. "We have let the Chamber know our position," says Rich A. Wells, vice-president for energy and climate change. So why not pull out? "They do other things for us, such as tort reform," he says. C.A. Howlett, a Chamber board member and senior vice-president for public affairs at US Airways, says that since "Tom [Donohue] came along, the Chamber's been completely revitalized." As for the recent uproar, he adds: "You can't make everybody happy all the time." | BW |

–With Theo Francis and John Carey in Washington


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THE SIDE EFFECTS OF FINANCE REFORM

Proposed rules aimed at curbing Wall Street abuses may crimp earnings and returns for investors, too

By Ben Levisohn and Mark Scott

Lawmakers and regulators across the globe are scrambling to corral banks and other culprits of the financial crisis. But companies and small investors may find themselves ensnared, too, because proposed and new rules could crimp corporate profits and investment returns.

Reformers aren't oblivious to the potential consequences. They just figure the benefits outweigh any side effects. Even so, says Simon Gleeson, a partner at law firm Clifford Chance, the perceived pitfalls "don't win politicians any gold stars for policymaking." And they won't make it any easier for companies and investors to dig out of the recession.

Consider the proposed rules for derivatives. Both U.S. and European regulators want to clamp down on the use of the complex financial instruments, whose values are tied to the performance of an underlying security or benchmark. The deals got a bad name last fall when an especially esoteric and risky version—credit default swaps—blew up, prompting huge losses at insurer American International Group and other companies. The pending reforms are meant to prevent another disaster.

But corporations could end up paying a price. Many companies buy basic types of derivatives to protect their earnings against fluctuations in interest rates, commodity prices, or currencies—a process known as hedging. "Hedging is an important weapon in any company's arsenal," says John Grout, policy and technical director at the Association of Corporate Treasurers, a trade group. American Airlines, for instance, controls its fuel costs with derivatives. Packaged goods maker Kraft Foods uses them to keep grain expenses in check.

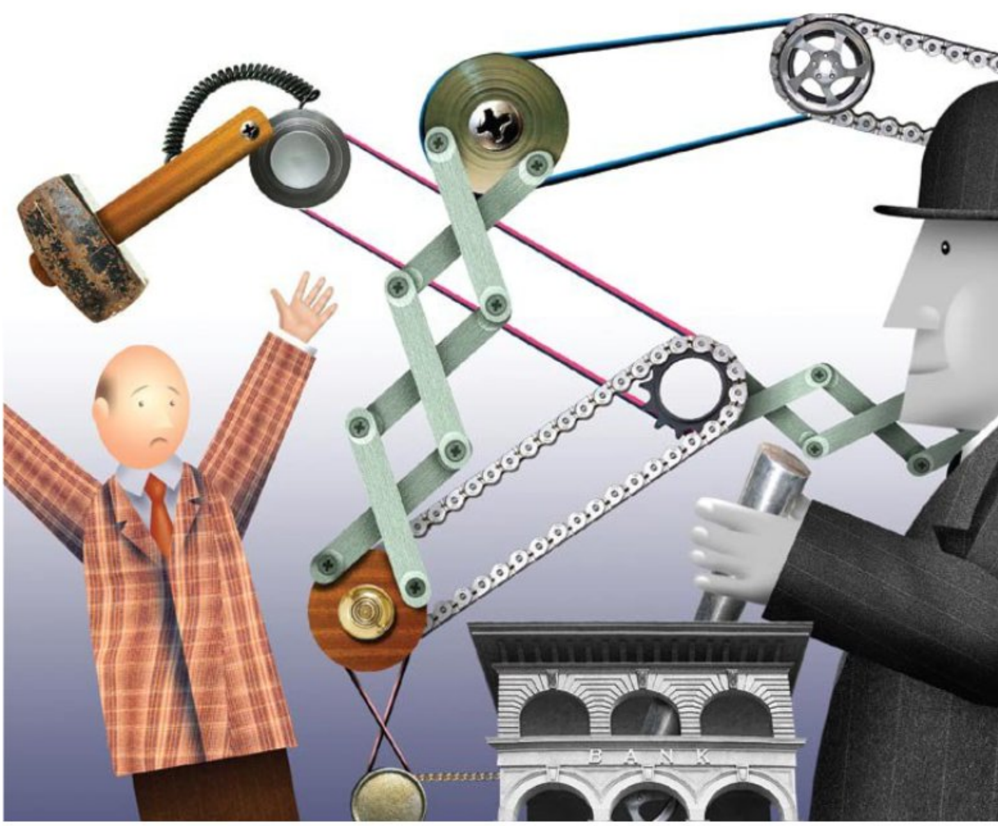
Any new rules may pressure companies to move their derivative deals to a regulated exchange, where trading is more transparent and oversight is stricter. (Right now almost all hedging contracts are created in private transactions with investment banks on the over-the-counter market.)

Exchange-based derivatives cut into cash reserves. Under current requirements, companies have to fork over 3% of a contract's value as collateral up front in case the transaction goes south. They also have to pony up extra funds should conditions change—say, when commodity prices rise or fall dramatically.

If the proposals go through, companies that use derivatives would have less money to invest in their operations. European manufacturing giant Siemens reckons it will need an extra $1 billion in cash reserves, and engine maker Rolls Royce figures its tab would total $4 billion.

The changes could also make derivatives a less effective tool for controlling expenses. Derivatives sold over the counter are tailored to a company's individual needs, while exchange-traded contracts are standardized. With custom contracts, corporations can lock in their prices through any date, say Dec. 12, 2010. A standard exchange contract only has certain dates—typically near the end of the month—leaving businesses vulnerable

ILLUSTRATION BY RAY BARTKUS



COLLATERAL DAMAGE

New regulations designed to rein in financial firms may affect companies and investors

AREA OF REGULATION	AIM	IMPACT
DERIVATIVES	Proposed rules seek to prevent another blowup in that market	Companies may pay extra for basic contracts
COMMODITIES	To stop speculators, regulators have limited holdings	Individuals have fewer investment choices
HIGH-FREQUENCY TRADING	Lawmakers may curb trading firms that use superfast computers	The cost of retail trading could rise

Data: *BusinessWeek*

to price movements in the interim. "Any reduction in the access to non-standardized derivatives would...add volatility and risk to quarterly earnings," Michael W. Connolly, Tiffany's treasurer, told Congress last month. The jeweler uses derivatives to manage the cost of silver and other metals.

Businesses are rethinking their strategies in response to the proposed rules. Some executives have stopped using these sorts of risk-management techniques for now, fearful that rule changes would void existing contracts.



Automakers and manufacturers, big users of derivatives, have been hesitant to enter into new deals because making changes to them could be costly. "It's causing treasurers to lose sleep," says Tim Sangston, managing director at consultancy Greenwich Associates.

Already the costs of derivatives are on the rise. As rivals get out of the business amid the tumult, JPMorgan Chase, Barclays, and others are hiking their prices. Banks now charge as much as 3% of a contract's value, compared with less than 0.1% before the crisis.

COMMODITY FUNDS SHUT DOWN

Meanwhile, individual investors are feeling the pinch from new regulations on commodities. The U.S. Commodity Futures Trading Commission and such exchanges as the New York Mercantile Exchange are limiting purchases of oil, grain, and other commodity derivatives known as futures contracts. The changes are designed to curb speculation by hedge funds and other financial players whose trading can affect the markets dramatically. Some experts suspect speculators pushed oil prices past $147 a barrel in 2008.

In light of the changes, financial firms are pulling back on some commodity offerings for small investors. On Sept. 1, Deutsche Bank announced it would shut down PowerShares DB Crude Oil Double Long, an exchange-traded product geared toward individuals. The bank figured it would be difficult to manage the fund without running afoul of the limits.

Money managers who keep their commodity funds open may decide to charge more or take bigger risks with exotic derivatives. Earlier this year the U.S. Natural Gas Fund, an exchange-traded offering, stopped issuing new shares amid worries about the limits. That drove up the value of existing shares, meaning investors who wanted access to the fund had to pay a 10% premium or more for their stakes. The fund recently started selling new shares again. To do so, the managers are buying complex derivatives, which introduces another set of problems. John Hyland, chief investment officer at the U.S. Natural Gas Fund, says the firm is taking steps to mitigate the risks, "but you don't eliminate them completely."

The regulatory environment has prompted some financial advisers to shy away from these types of offerings. Barclays Wealth recently told high-net-worth clients to ditch exchange-traded funds that focus on commodities in favor of hedge funds and other alternatives that invest in this area. "Most ETFs are still O.K.," says Michael Crook, a strategist with Barclays Wealth. "We just don't know what's going to happen."

Retail investors may also take a hit if high-frequency trading is curbed. The Securities & Exchange Commission is investigating whether financial firms that use superfast computers to buy and sell stocks have an unfair advantage. The technique has been controversial of late as big trading firms have booked billions in profits while their clients' portfolios have dwindled.

If the SEC cracks down on the practice, trading costs may rise. High-frequency traders buy and sell stocks in small lots regularly throughout the day. Their activity, roughly 70% of market volume, has helped drive down spreads—the difference between the price at which a stock is bought and the price at which it is sold. A decade ago, the spread for retail investors was roughly 6¢ a share. Now it's around a penny. "With any new technology, there's always the possibility of misuse," says Andrew W. Lo, a professor at Massachusetts Institute of Technology's Sloan School of Management. "But investors are benefiting from it." |BW|

A TOUCHDOWN FOR COMCAST?

Wall Street may not like the cable giant's bid for NBC Universal, but it could make sense



Roberts could create a strong rival to ESPN with NBC's sports programming

BILL CRAMER/WONDERFUL MACHINE

By Ronald Grover and Tom Lowry

It's become an almost Pavlovian response among Wall Street analysts and money managers: holding their noses when an executive proposes bringing content (movies and TV shows) and distribution (cable, satellite, and Internet) under one roof.

And so when investors learned on Sept. 30 that Comcast CEO Brian L. Roberts was considering a deal to take majority control of General Electric's NBC Universal (NBCU), the cable giant laid an egg on Wall Street. Its share price fell 7% the next day, to 15.67. The Street's worry was clear: Roberts' yen for NBCU's movies and TV shows would divert his executive team from the core business of providing cable TV, broadband, and phone service to Comcast's nearly 25 million subscribers.

Roberts has had a bad rap on Wall Street ever since 2004, when the cable company bid $54 billion for Walt Disney and then walked away once the Mouse House played hard to get. Roberts is mindful of that and of the Street's obsession with quarterly numbers. But he also needs to manage for the long haul. That means finding a way to offset slowing growth at Comcast, which is losing subscribers to phone and satellite companies and could suffer as more viewers move to the Web to watch movies and TV shows. (Roberts declined to comment.)

The NBCU deal could give a slowing Comcast a significant lift. People with knowledge of Roberts' thinking single out NBC's sports assets. The Peacock Network controls the rights through 2012 for the Olympics and through 2013 for Sunday night National Football League games. With NBC's high-end sports, Roberts could build Comcast's smallish Versus sports channel into a bigger player. And with the NFL as a partner, Roberts could be in a position to pressure the league to cut him in on an even more robust deal to carry more football games.

–7%

Change in the share price of Comcast on news it might take control of NBC Universal

Data: Bloomberg

HAVING A SAY IN HULU

With NBC, Roberts will "have effectively created a potent competitor to ESPN," says Neal Pilson, a former CBS sports executive who now consults. Pilson figures Comcast will use NBC Sports' national platform to complement its 11 regional sports networks, which include major markets such as New York, Chicago, Philadelphia, and San Francisco. Throw in Comcast's Golf Channel and Versus, which has college football and pro hockey games, and the new entity clearly would give agita to executives at ESPN headquarters in Bristol, Conn.

With access to NBC content, Roberts could enhance his current cable offerings by providing more shows to subscribers over the Net—and eventually via their smartphones. Comcast already has Fancast, a free video site that doesn't have much traction. By controlling NBC, he'd have a say in the future of the much more popular Hulu online video service, which NBC co-owns with Fox and Disney. Roberts might want to charge everyone access to Hulu, which currently is free, and take a cut of the proceeds.

Assuming Roberts wins control of NBC, the network likely wouldn't look the same for long. Federal regulators almost certainly would force Comcast to sell off TV stations in markets in which it also owns cable systems. The next logical step? Converting NBC into a cable channel. That would allow Comcast to charge cable and satellite operators hefty fees for the privilege of carrying NBC shows, giving Comcast a way to offset falling advertising revenue.

For Brian Roberts, there is no shortage of potential. First, of course, he has to get his hands on NBC Universal. And then he has to change the minds of shareholders who have long worried that the Comcast CEO covets Hollywood flash over cable's fundamentals. But even those opinions may be changing. "It's a very good deal for Comcast," says media investing heavyweight Mario Gabelli, whose fund owns some 22 million Comcast shares. "It's a win-win for Brian." | BW |

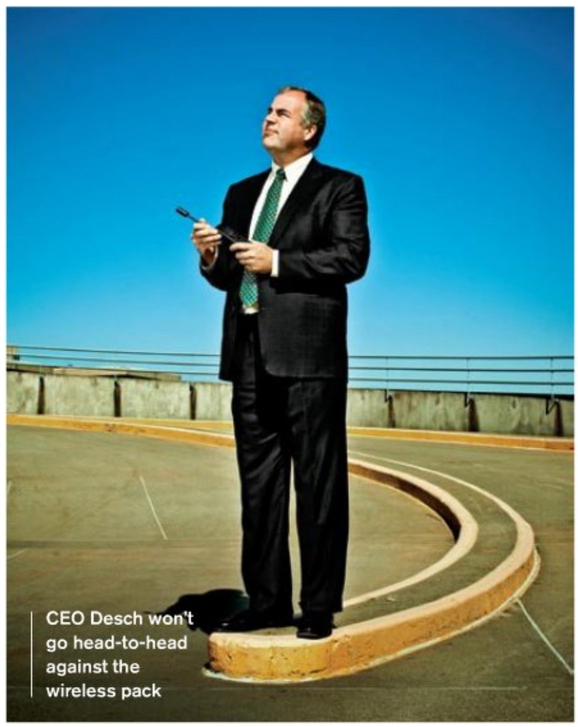
THE SECOND COMING OF IRIDIUM

The satellite phone company, which flopped in 1999, is back and planning to tap new markets

By Arik Hesseldahl

Ten years after suffering one of tech's most spectacular flameouts, satellite phone service Iridium Communications is staging a comeback. Its late-September public share sale has sparked hope for the broader satellite industry, long burdened by exorbitant startup costs and anemic demand.

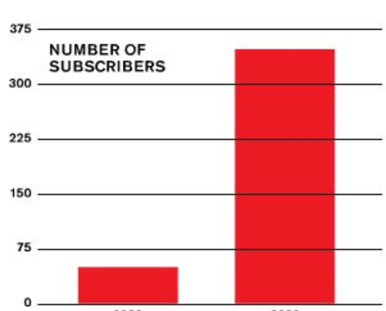
Iridium raised $200 million in a Sept. 29 initial public offering after reinventing itself and earning $54 million on $320 million in sales last year. The company initially planned to provide calling service for on-the-go executives using signals beamed from 66 orbiting satellites.



CEO Desch won't go head-to-head against the wireless pack

Iridium, then backed by Motorola, planned to go head-to-head with cellphone carriers that charged high fees for out-of-network calling. But the idea was rendered largely obsolete as mobile-phone carriers expanded their reach and cut deals among themselves to allow calls over rival networks, making service cheaper. Iridium lured too few subscribers and sought bankruptcy in 1999 after racking up more than $2 billion in losses. Three years later rival Globalstar followed suit, while the same year Teledesic, founded by wireless impresario Craig McCaw and Microsoft founders Bill Gates and Paul Allen, closed.

THEN AND NOW



Data: Iridium

WHERE MOBILE WON'T GO

Iridium still provides satellite calling, but plans to tap new markets and run satellites more cheaply. After emerging from Chapter 11 in 2001, it has amassed 347,000 customers. "People understand much better what these things cost, how they work, and what they can and can't do," says Jonathan Atkin, an analyst at RBC Capital Markets, which worked on Iridium's IPO.

For Iridium and other satellite companies, the challenge is translating that realism into profits. Now Iridium wants to provide communication in areas not reached by mobile networks. "Less than 10% of the earth's surface has wireless coverage," says Iridium CEO Matthew J. Desch. Target regions include the sea and mountains—places where governments and oil and shipping companies will pay dearly for coverage.

The U.S. military is Iridium's largest customer, making up about 21% of revenues. "This is the very definition of a niche product," says Chris Quilty, an analyst at Raymond James, co-leader of Iridium's IPO. "It's used by people who need to have it."

Still, Iridium's voice business may grow at less than 10% a year, Quilty says. So Iridium is also pursuing so-called machine-to-machine (M2M) communications, where machines beam data back and forth via satellite. Companies use M2M tech to monitor remote equipment and track shipments.

The company's biggest financial hurdle will be to replace aging satellites beginning in 2014 at a total cost of $2.7 billion. To pay the bill, Iridium will issue debt and tap IPO proceeds.

Iridium plans to raise "hundreds of millions" in additional funds, Desch says, by leasing space on its satellites. Rival Intelsat, for example, was paid $167 million by Australia's Defence Force to piggyback on a satellite covering the Asia-Pacific region.

If all else fails, Iridium may be able to fall back on its No. 1 customer. The U.S. Defense Dept. plans to deploy the company's technology in new navigation gear and in a secure walkie-talkie system. "The military bought into the Iridium concept in the 1990s," says Raymond James' Quilty. "If everything hits the fan again, they'll still have their buddies at the Pentagon." |BW|

STEPHEN VOSS

SONY'S GOOGLE GAMBIT

It is latching onto the search giant's open-source Android and other offerings as it plays catch-up with competitors

By Kenji Hall
TOKYO

It's starting to look like more than a schoolyard crush. As Sony scrambles to recover from billions of dollars in losses, a flirtation with Google is becoming serious. It's the first PC maker to sell machines preloaded with the search giant's Chrome Web browser; the Sony Reader will be able to download e-books in a format backed by Google; and Sony Ericsson cell phones will use Google's Android operating system.

Google may be less excited about the tieups than Sony is, but the advances aren't likely to go unrequited. Last winter, Sony invited Google executives to Tokyo for discussions on integrating Android and other Google offerings into Sony's gadgets, according to a person with knowledge of the meeting. "Sony believes Google's products and software can help differentiate it from competitors," says Tim Bajarin of tech consultancy Creative Strategies.

While Sony officials declined to comment, closer ties with Google clearly fit into the Japanese company's ambitions in software. For decades, Sony has excelled at making gadgets, but it has lagged in linking them to each other and to the company's music, movies, and TV shows. To speed that process, Chief Executive Howard Stringer four years ago put Apple veteran Tim Schaaff in charge of software. Last February, Stringer reshuffled top management, turning to younger executives who are, he said at the time, "network-centric and very open-minded." Cozying up to Google helps Stringer speed development of products that can tap into the Web.

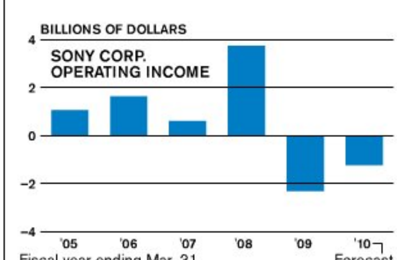
The moves are part of a shift toward open-source software at Sony. The Web has been flooded with photos of a Sony Ericsson touchscreen phone running Android, an open-source operating system. Sony recently introduced a global-positioning device that synchronizes with Google Maps to pinpoint where photos are taken, and it's now offering a video camera that lets users quickly upload clips to YouTube. The company says it also may let Google and others create applications for its PlayStation 3 game console. "Open technologies are very important to consumers," Schaaff said in an interview last year. "Obviously we don't have a monopoly on innovation."



It's too early to say whether the strategy will pay off for Sony. Android alone won't automatically make Sony's products easier to use or more compatible with each other. And there's a risk that Sony's offerings will start to look more like those from rivals. Samsung, HTC, and Motorola already have smartphones running Android, and Hewlett-Packard and Asustek Computer are considering it for mini laptops. And there's little to stop others from offering the Chrome browser or compatibility with Google's book format on their devices. "Gaining competitive advantage from open-source software is difficult because it is available to competing manufacturers," says iSuppli analyst Matthew Wilkins.

Still, using Chrome may restore some cool to Sony's brand. Android gives Sony instant access to an online store where independent developers sell thousands of applications. That would allow the company to compete with similar services from Apple, BlackBerry, Nokia, and Microsoft. And in digital books, the Reader will have an edge on Amazon's Kindle, which can download content only from Amazon.com. "Sony knows it can't assign enough people to work on all these things," says Richard Doherty, research director at Envisioneering Group, a technology consultancy in Seaford, N.Y. "It can't do it alone." BW

TIME FOR A REBOOT?



Fiscal year ending Mar. 31

Data: Sony

ILLUSTRATION BY ROBERT NEUBECKER; CHART BY ALBERTO MENA/BW



BREITLING
PROFESSION: PILOT CAREER: ACTOR
People are acquainted with the star, the multi-faceted actor. But John Travolta is also a seasoned pilot with more than 5,000 flight hours under his belt, and is certified on eight different aircraft, including the Boeing 747-400 Jumbo Jet. He nurtures a passion for everything that embodies the authentic spirit of aviation. Like Breitling wrist instruments. Founded in 1884, Breitling has shared all the finest hours in aeronautical history. Its chronographs meet the highest standards of precision, sturdiness and functionality, and are all equipped with movements that are chronometer-certified by the COSC (Swiss Official Chronometer Testing Institute).
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THE LOST GENERATION

By Peter Coy
Photograph by Jennifer S. Altman

The continuing job crisis is hitting young people especially hard—damaging both their future and the economy

Bright, eager—and unwanted. While unemployment is ravaging just about every part of the global workforce, the most enduring harm is being done to young people who can't grab onto the first rung of the career ladder. ¶ Affected are a range of young people, from high school dropouts, to college grads, to newly minted lawyers and MBAs across the developed world from Britain to Japan. One indication: In the U.S., the unemployment rate for 16- to 24-year-olds has climbed to more than 18%, from 13% a year ago. ¶ For people just starting their careers, the damage may be deep and long-lasting, potentially creating a kind of "lost generation." Studies suggest that an extended period of youthful joblessness can significantly depress lifetime income as people get stuck in jobs that are beneath their capabilities, or come to be seen by employers as damaged goods.

Equally important, employers are likely to suffer from the scarring of a generation. The freshness and vitality young people bring to the workplace is missing. Tomorrow's would-be star employees are on the sidelines, deprived of experience and losing motivation. In Japan, which has been down this road since the early 1990s, workers who started their careers a decade or more ago and are now in their 30s account for 6 in 10 reported cases of depression, stress, and work-related mental disabilities, according to the Japan Productivity Center for Socio-Economic Development.

When today's unemployed finally do get jobs in the recovery, many may be dissatisfied to be slotted below people who worked all along—especially if the newcomers spent their downtime getting more education, says Richard Thompson, vice-president for talent development at Adecco Group North America, which employs more than 300,000 people in temporary positions. Says Thompson: "You're going to have multiple generations fighting for the jobs that are going to come back in the recovery."



Dan Schmitz, 25, a University of Wisconsin grad, hasn't had a job in months

What's more, the baby boom generation is counting on a productive young workforce to help fund retirement and health care. Instead, young people risk getting tracked into jobs that don't pay as well, says Lisa B. Kahn of the Yale School of Management. That would mean lower tax payments for Social Security and Medicare.

Only 46% of people aged 16-24 had jobs in September, the lowest since the government began counting in 1948. The crisis is even hitting recent college graduates. "I've applied for a whole lot of restaurant jobs, but even those, nobody calls me back," says Dan Schmitz, 25, a University of Wisconsin graduate with a bachelor's degree in English who lives in Brooklyn, N.Y. "Every morning I wake up thinking today's going to be the day I get a job. I've not had a job for months, and it's getting really frustrating."

ANXIETY AND FEAR

The case for action is strong. Governments should act now before the damage gets even worse, argues David G. Blanchflower, an economist at Dartmouth College who recently served on the Monetary Policy Committee of the Bank of England. He's not sure what will work, but he favors trying everything from subsidizing education and training to cutting minimum wages for young people and trainees. "It has to be

now," says Blanchflower. "It can't be in two years' time."

Most analyses of youth employment focus on people aged 16 to 24, which includes everyone from high school dropouts to wet-behind-the-ears college grads. But in this era of rising educational requirements, some people don't start their careers until their mid or late 20s—and these young college grads are taking it on the chin as well.

According to a *BusinessWeek* analysis, college graduates aged 22 to 27 have fared worse than their older educated peers during the downturn. Two years ago, 84.4% of young grads had jobs, only somewhat lower than the 86.8% figure for college graduates aged 28 to 50 (chart). Since then, the employment gap between the two groups has almost doubled.

Robert I. Sutton, author of *The No Asshole Rule*, a management book, says he's seeing "more anxiety and fear" among his students at Stanford University. At Northwestern University Law School, at least three-quarters of students who graduated in May had their employment deferred, in some cases up to a year, says Bill Chamberlain, head of the school's career center.

But the situation is most severe for job seekers who lack college diplomas and thus have fewer options. "My friends tell me: 'Go fill this out. Go do that,'" says Charlie Black, 26, of Manhattan, who was out one recent weekend shopping for a Halloween costume for his 2-year-old daughter, Bree. Black has been a union extra in several TV shows and movies, and for a year he worked the overnight shift at an Abercrombie & Fitch store. Now, jobless for almost a year, he would be happy to work as a janitor. "But no jobs have been calling back," says Black.

It seems strange at first blush that young people are the biggest victims of the current economic slump. One could easily imagine that companies in a recession would prefer to hire young people, who are cheap, and slough off older workers, who are expensive. But both employers and older workers are sitting tight, taking as few risks as possible in an uncertain environment. With no openings, employers are refusing even to look at the résumés of those on the outside looking in.

The sense of stasis in many Western countries is reminiscent of Japan, where talk of a lost generation has been around since as long ago as 1995. Some 3.1 million Japanese aged 25 to 34 work as temps or contract employees—up from 2 million 10 years ago, according to the Ministry of Internal Affairs.



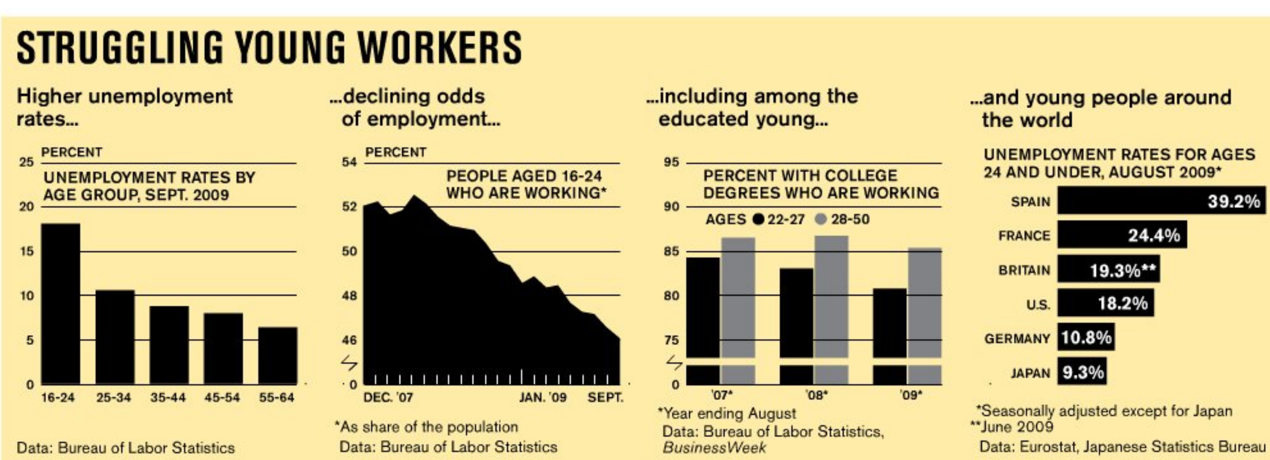
"No jobs have been calling back," says 26-year-old Charlie Black of Manhattan



Many Japanese blame the young people themselves, saying they are spoiled, alienated "freeters"—a term meaning job-hopping part-timers. But economist Souichi Ohta of Nagoya University argues that a big part of the problem is Japanese employers, who value long experience at their companies—which newcomers by definition don't have.

Europe offers different lessons about what to avoid. In Spain, employers generally put older workers on long-term contracts that are hard to break. When demand slumps, they get rid of the younger workers, notes Alfredo Pastor, an economist at Spain's IESE Business School and former Spanish Secretary of State for the Economy. That's one reason Spain's unemployment rate for 16- to 24-year-olds is a sky-high 39%. The rate is 24% in France and 19% in Britain.

Economists in several countries have studied the damage such high unemployment can cause. Kahn of Yale found that



PHOTOGRAPH BY JENNIFER S. ALTMAN; CHARTS BY LAUREL DAUNIS-ALLEN/BW



Shireen Rahjou, 23, of Boca Raton, Fla., has landed a paid internship at a PR firm

JEFFERY SALTER/REDUX

graduating from college in a bad economy has a long-lasting negative effect on wages. For each percentage-point rise in the unemployment rate, those who graduated during the recession earned 6% to 7% less in their first year of employment than their more fortunate counterparts. Even 15 years out of school, the recession graduates earned 2.5% less than those who began working in more prosperous times.

SUBMINIMUM WAGE?

What can be done? For one thing, companies should keep hiring young people even if they're doing layoffs. That's how General Electric operates, says Susan P. Peters, the company's vice-president for executive development. She says GE learned from the mistake of its aviation business, which froze hiring and training during a downturn years ago and found its talent pipeline dry when business recovered. "We tell our businesses, 'Tough, you have to hire,'" Peters says.

Free-market economists favor removing obstacles to employment of the young, such as high minimum wages. "The government in some ways is contributing to this problem," says Kristen Lopez Eastlick, senior research analyst for the employer-backed Employment Policies Institute. She points out that the 40% hike in the federal minimum wage over the past two years made it less appealing to hire young workers. One possibility: Some U.S. states and European countries have enacted subminimum wages just for young people or people enrolled in apprenticeships.

More job training would help as well. In April the British government guaranteed that starting next January, all people under age 25 who have been unemployed for more than a year will have a job offer, training, or a paid workplace experience.

The U.S. has been slower to beef up job programs for the young, partly because of massive budget deficits. The Obama Administration is again considering a plan proposed during the campaign to give $3,000 tax credits to employers for each new hire, although an Administration spokesman says talks with Congress are only preliminary. An argument in favor of action: The current generation of young people is larger than the one that follows. Dartmouth's Blanchflower points out that even if programs are left in place after the recession ends, they will serve fewer people and therefore become less costly.

One possible example for the U.S. to follow is Germany's apprenticeship program, which guides young people from high school into skilled blue-collar jobs. Young-adult unemployment in Germany has risen less than in most other developed countries (page 36).

Young people have figured out how to avoid horrid blanks on their résumés. Enrollments are breaking records at such schools as Cincinnati State Technical & Community College and LaGuardia Community College in New York. With no job in sight, Shireen Rahjou, 23, of Boca Raton, Fla., is working toward a master's degree in public relations. She recently landed a paid internship—O.K., not a job, but a foot in the door—at a PR firm in Miami.

With jobs scarce, Stanford's Sutton says some of his students plan to start their own businesses. Schools should encourage that instead of churning out "passive regurgitators," argues Kate McKeown, an adjunct professor of entrepreneurship at Fordham University's College of Business Administration.

Meanwhile, though, the tide of youth unemployment keeps rising. "We're seeing further deterioration," says Stefano Scarpetta, who heads the employment-analysis division of the Organization for Economic Cooperation & Development, a forum for rich countries.

The unemployment crisis among the young is not as dramatic as the financial crisis of a year ago. But it may turn out to have longer-lasting effects. |BW|

—With Mark Scott in London, Ellen Gibson and Lindsey Gerdes in New York, Carol Matlack in Paris, and Kenji Hall in Tokyo

Business Exchange

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Tackling the Job Crisis

The system for moving young people into the workforce was functioning poorly in many nations even before the global economic downturn began, says a new report from the Organization for Economic Cooperation & Development. The 26-page report, called "Helping Youth to Get a Firm Foothold in the Labour Market," was prepared for an OECD meeting in Paris on Sept. 28-29. The most urgent priority is to prevent unskilled dropouts from losing touch with the workforce altogether, according to the report. "For disadvantaged youth lacking basic education," the document says, "a failure in their first experience on the labor market is often difficult to make up."

To view the report, go to **http://bx.businessweek.com/unemployment/reference/**

GERMANY'S ANSWER: THE APPRENTICE

How a system of vocational training reduces youth joblessness

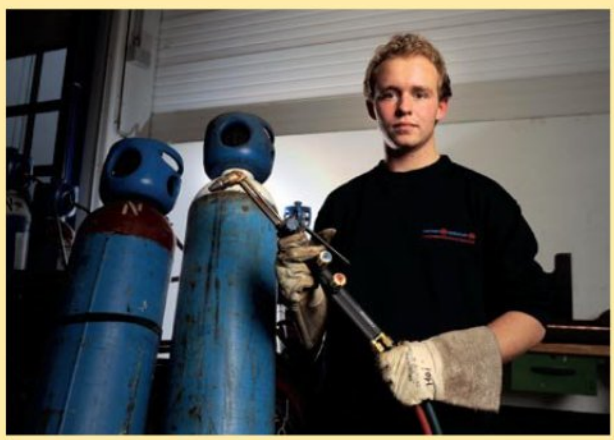
By Jack Ewing

In most countries, giving up full-time schooling at age 15 would seem like a bad plan. But for Christian Dietrich, who lives in the German village of Ketsch, outside Heidelberg, the move made sense. Three years ago, Dietrich became an apprentice at Helmut Herbert, a large plumbing contractor in nearby Bensheim, alternating two weeks of on-the-job training with one week of classes at a vocational school. Now 18, Dietrich will qualify next year in what are traditionally separate trades: heating, plumbing, and air-conditioning. He's proud of his accomplishment. "You used to have to call three technicians. Now you only need one," says Dietrich, already making a sales pitch for his employer.

Germany's apprenticeship system offers one model of how to hold down youth unemployment, especially among the less well-educated. Under-25 joblessness was 10.8% in August, according to Eurostat, roughly half the European Union average. Austria, Denmark, and Switzerland also have well-established apprenticeship programs and lower-than-average youth unemployment. Rather than floundering after high school, young workers are plugged right into the labor market.

Companies are happy with the system, too. Apprenticeships give employers several years to train workers in company-specific skills and assess the abilities of an *Azubi*—short for *Auszubildener* (trainee). Says Günther Hohlweg, who oversees the 10,000 young people learning trades at Munich-based electronics and engineering giant Siemens: "When they're done, they can start on a higher level."

The system is even good for the national budget, because companies bear much of the cost of secondary-school education. German authorities accredit some 350 kinds of apprenticeship, ranging from baker to hair stylist and bank clerk to video editor. Even university students may be apprentices, splitting their time between studying and gaining practical experience in fields such as biotech or aerospace.



Dietrich, 18, is learning heating, plumbing, and air-conditioning

Lately, though, the system has come under stress because of factors related to both the current downturn and long-term changes in the global labor market. The number of apprenticeships slumped more than 10% between 2000 and 2005, recovering only after the government threatened to compel companies to take more trainees. German officials expect the number to dip again this year because of the financial crisis. Although apprentices in lower-skilled trades can serve as cheap labor, they are often an expense to their employers in the short term. Siemens (page 17) spends about $220 million a year training *Azubis*, some of whom earn as much as $1,500 a month. The company estimates that the productive work done by the trainees equals only about one-third their cost. Siemens, which offers almost all its apprentices full-time jobs, recoups the investment only later.

The biggest problem is a shortage of work for teens who complete only basic schooling, which may end after the ninth grade. Germany's highly automated factories offer far fewer low-skilled jobs than they used to. As a result, more than half the graduates of basic schooling wind up in government-supported training programs. The 25% who don't land a private-sector apprenticeship run a high risk of long-term unemployment. "Because of the changes in the labor market, the system is not functioning as smoothly as it used to," says Tilly Lex, a sociologist at the German Youth Institute who studies job training.

At the same time, some industries take on too many apprentices. Hair salons, for example, can profit from the cheap labor that trainees provide. So they tend to train more hairdressers than the market can absorb. Once young people have invested years learning a trade, it's tough to start over. Germany is much less successful retraining older workers than training young ones.

The big question is whether the apprenticeship program is flexible enough to adjust to a changing global economy. Says Markus Kiss, an education specialist at the German Chamber of Commerce & Industry: "The system has a future, but it has to be adjusted." |BW|

MARCUS THELEN



FOOD COMPANIES COME TO THIS FRENCH VILLAGE TO WORK ON SECRET RECIPES.

BUT YOU DIDN'T HEAR IT FROM US.







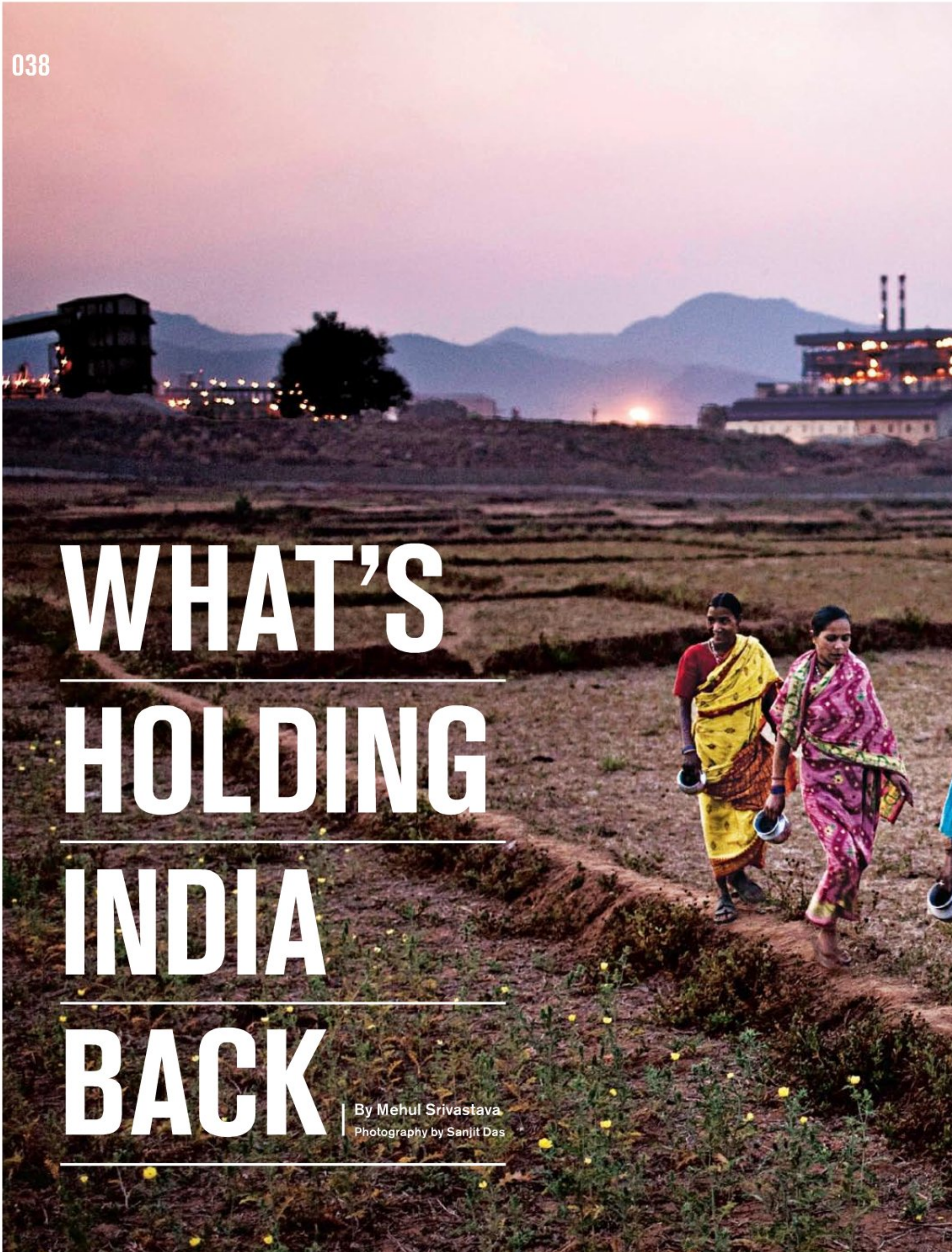
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WHAT'S HOLDING INDIA BACK

By Mehul Srivastava
Photography by Sanjit Das



Business is battling farmers over land, putting $98 billion in investments—and an industrial revolution—on hold

Spitting a fine stream of red betel-leaf juice into the knee-deep waters of his rice paddies, Subhash Mahapatra points to the line dividing his land from his neighbor's. It's not much, but his family has cultivated rice on the two acres of dark, loamy soil for generations, and Mahapatra knows of no other way to feed his children. "If I don't want to sell it, do I not have the right to say no?" he asks. ¶ The answer to that question may determine whether India will see a new industrial revolution, one broad enough to provide the jobs needed to lift millions out of poverty. Mahapatra's property is part of a 4,000-acre parcel that the government of Orissa state five years ago promised to steelmaker Posco. The South Korean giant had hoped it would be home to India's biggest steel

Vedanta's aluminum plant in Orissa can't yet use locally mined bauxite

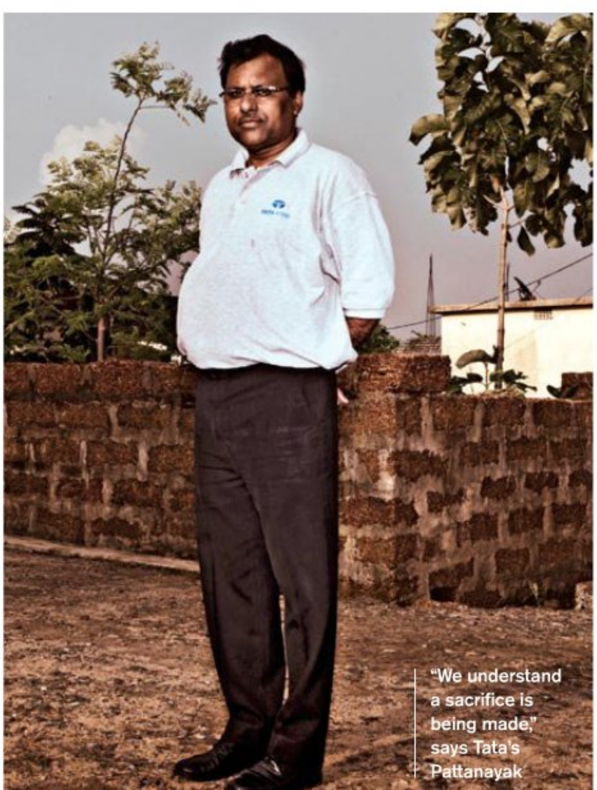


mill, a $12 billion behemoth with its own port on the Bay of Bengal. So far, Posco hasn't even managed to build a fence around the site, as Mahapatra and thousands of others have battled police, once even taking Posco workers hostage for a few hours.

Across India, similar struggles are holding back nearly 200 proposed factories, railroads, highways, and other projects. Add it up and you'll find that some $98 billion in investment is in limbo, the Association of Indian Chambers of Commerce estimates. On Oct. 5, Luxembourg-based ArcelorMittal said problems getting land may force it to reconsider a $20 billion plan to build two steel mills near the Posco site. Automaker Nissan-Renault, London-listed metals giant Vedanta Resources, and Indian outsourcing stars Infosys and Wipro have all seen initiatives scuttled or delayed by troubles in acquiring land. "All I want to do is build a steel plant," says Gee Won Sung, Posco's India director. "If we can, a whole city will be created," says Sung, his voice barely registering in the air-conditioned conference room on the sixth floor of the company's glass-fronted office building in Orissa's capital, Bhubaneswar. "In 10 years, this whole region would change."

That requires convincing Mahapatra and his neighbors to move. Under Indian law, the answer to Mahapatra's question is clear: He doesn't have the right to say no once the state has decided to acquire his land. But under Indian reality, there's not much Posco or the government can do if Mahapatra stays put. Politicians hate the idea of evicting voters, and riots have broken out when surveyors show up with measuring gear. In Mahapatra's village, locals stand guard at a gate they erected, ready to fight any effort to move them out.

Mahapatra: "If I don't want to sell, do I not have the right to say no?"



"We understand a sacrifice is being made," says Tata's Pattanayak

ADVANTAGE CHINA

A proposed expansion of Mumbai's airport has been slowed because the runways abut a slum that residents refuse to vacate. Tata Motors halted construction on a factory for its $2,500 Nano subcompact in West Bengal state after locals blockaded the site for months. The company finally decided to build the plant 1,300 miles away, in Gujarat. On the beaches of Goa, fishermen heckle Environment Minister Jairam Ramesh when he defends moving them from the coast to make way for resorts that charge foreigners $400 a day to sunbathe on fenced-off stretches of sand.

If these problems can't be resolved, India will be hard-pressed to create the kind of sustainable economic growth enjoyed by its giant neighbor, China. Some 280 million Chinese work in factories; fewer than 45 million Indians do so, and India's industrial output is about the same as Spain's. "People who've gotten a little too excited about the India story seem to have forgotten that without solving a basic issue like land, it's difficult to see the country having any sort of industrial revolution," says Robert Prior-Wandesforde, senior Asia economist at bank HSBC.

With its anemic manufacturing base, India's economy offers scant opportunities for the rural poor. Cities such as Bangalore and Mumbai have been transformed by tech services, but fewer than 10 million people work in that sector. India's largest employer is its fields, where some 550 million farmers such as Mahapatra toil in conditions little changed for centuries. "There's nothing here," Mahapatra says as his daughter-in-law prepares a meal of rice, lentils, and vegetables in the two-room hut shared by his extended family of nine people. "Jobs? Development? I was born a farmer, and I will die one."

Finding new homes for farmers lies at the heart of the dispute. Under Orissa law, the displaced are given small plots elsewhere—but never more than five acres, regardless of the amount of land acquired by the government. Other provisions include employment for one member of the family, up to $500 in cash for job training, and help building a new house. "We understand a

BOGGED DOWN

Indian manufacturing projects facing delays due to land acquisition

COMPANY
INVESTMENT
STATUS



sacrifice is being made," says P.K. Pattanayak, who is overseeing development of a $4.5 billion mill that Tata Steel wants to build in eastern Orissa. "Unless villagers are convinced that we are sincere in our efforts to care for them, I don't think any industry can move forward."

Indian farmers have reason to be wary. While governments offer what they call the going rate for property, in much of rural India—where most people are subsistence farmers—there are so few transactions that establishing a market value for land is virtually impossible. From 2001 to 2007, 1.4 million residents of Orissa and three neighboring states were displaced after their land was acquired by the government or companies, the Rural Development Ministry says. Most of them ended up unemployed, and 90% say they received too little compensation, according to a report by Delhi's Indian Social Institute and London-based ActionAid.

The disputes can last years. In 1991, Orissa started to assemble land for the industrial zone where Tata Steel would eventually seek to build its mill. At the time, the state offered Chakradhar Haibru $1,400 for his two acres, though he was allowed to stay on until an industrial tenant was found. The 70-year-old farmer, frail and illiterate, thought the price was laughable and never cashed the check. Today he leads his neighbors in opposing Tata. "My family has lived here since 1860," Haibru says in the dusty courtyard of his home, a stone's throw from a monument to 12 protesters killed by police during a 2006 riot over land. "And because Tata wants to build a plant here, I must move. Where do I go?"

To see where he might go, drive the 10 miles to one of Tata's resettlement colonies. Each of the 700 families that agreed to move out got a tenth of an acre, about $3,000 to build a house, and either training for a job or a one-time payment of $4,500.

ArcelorMittal	Posco	Vedanta	Jindal Group	Tata Steel	GMR Energy	Nissan
$20 billion	$12 billion	$9 billion	$5 billion	$4.5 billion	$1.2 billion	$1.1 billion
Two mills delayed at least two years; may be relocated	Three-year-plus delay; no construction started	Three-year delay getting land for mine; nearing completion	Two steel mills in eastern India delayed more than a year	Two-year-plus delay on mill in Orissa; some land acquired	Year-long delay on power plant; still has just 70% of land	Projects with two local partners delayed over a year



Vedanta's Kumar says its plant will "create opportunities" for local residents

Some 80 brick-and-mortar houses line dusty streets where children play catch and unemployed men linger in the doorways. "I miss the village life, my old home," says Lakshmi Mohanto, whose family sold six acres to the state for Tata to use. "But this is a nice house."

She's among the lucky ones. Eager to convince Haibru and others to make way for the Tata mill, the company has been relatively generous to those who have moved. Less fortunate are the 196 people who have lived in a Posco transit camp since agreeing to sell their land to the Koreans. Though they haven't yet gotten paid for their property—in fact, no price has been set—they say they have been threatened by neighbors for supporting Posco. But until Posco breaks ground on the mill, the company says, it has no plans to build permanent homes. Santosh Mohanty, 26, has shared a one-room shack with his parents and a brother for more than a year. With no work, the family scrapes by on a Posco handout of $1.60 a day. Asked if he is happy with his decision to sell, tears well up in Mohanty's eyes. "No," he says.

Mohanty's plight highlights the other roadblock to resettlement: finding jobs for those who have always lived off the land. Tata Motors' Nano factory in West Bengal, for instance, would have required some 8,000 people to move, but it would have created fewer than 1,000 jobs, most requiring skills few farmers have. So an Indian industrial revolution could end up displacing many more people than it employs.

LAND TITLES IN QUESTION

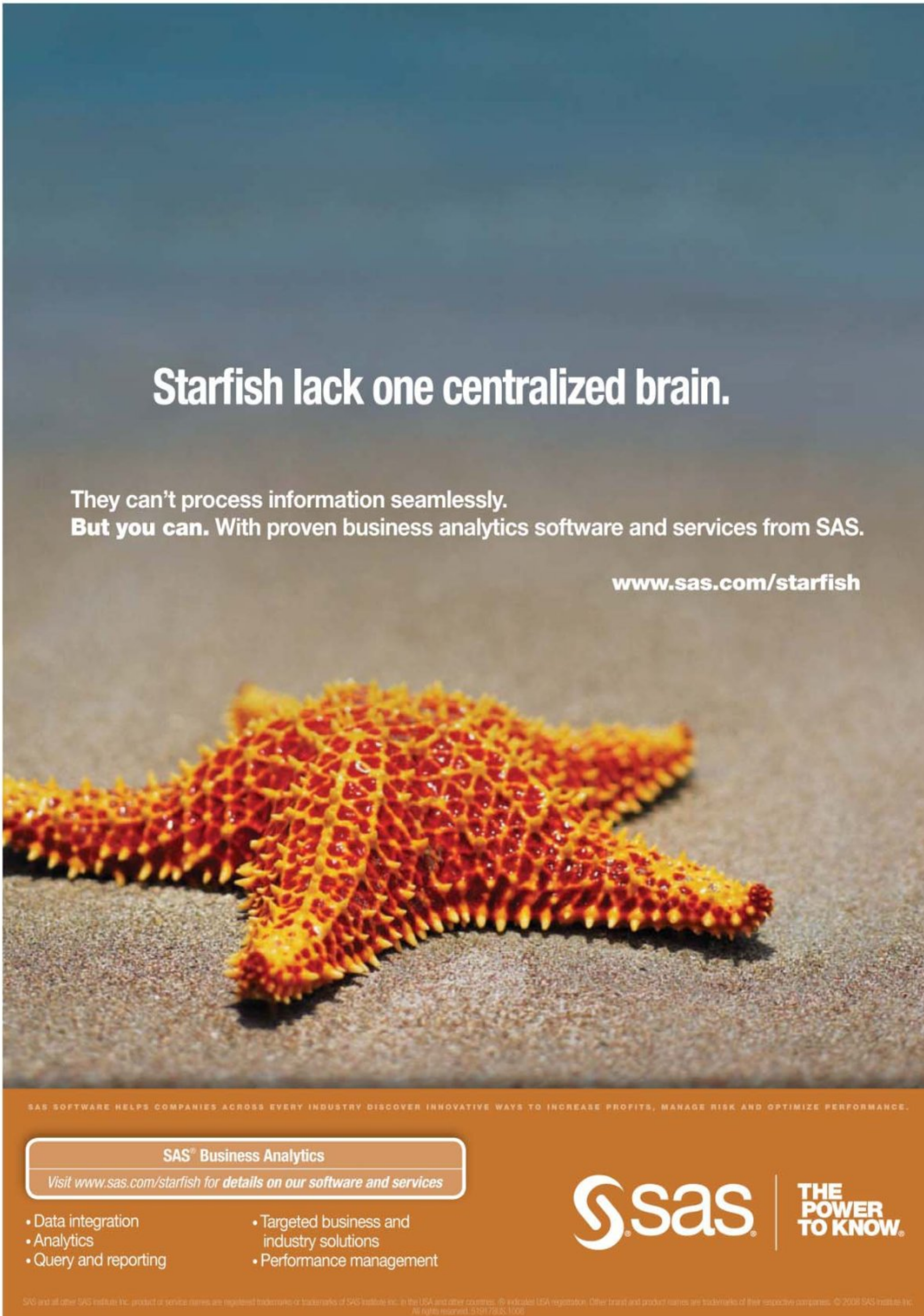
Farmers feel they could get a better price by dealing directly with companies rather than with government development agencies, whose offers are nonnegotiable. That may happen more often if a bill being considered in Delhi makes it through Parliament. Under the measure, companies would be required to reach agreement with individuals for 70% of the land for any project, setting a fair value for the property. Then the government would step in to force any holdouts off the remaining 30%, paying the established price rather than the low rates many owners are offered today. But land title in India is difficult to trace, and it's unclear whether those who work the land but don't own it—often 80% of the displaced—will get anything.

A few companies are willing to put in the hard work—and hard cash—needed to cut deals with individuals. Not far from Tata Motors' proposed plant in West Bengal, JSW-Bengal Steel acquired 4,860 acres in 2008. The company paid farmers $6,400 per acre—three times what the government said the land was worth—and threw in another $6,400 in company shares, which the farmers can sell when the mill is completed in 2011 or 2012. "We started with a simple realization: For a farmer, his connection to land is like an umbilical cord," says Biswadip Gupta, chief of JSW-Bengal Steel. "Unless you can get landowners on your side, there's no point in even trying [to build a factory]." In 2007, when the government of Haryana state, outside Delhi, offered little help to Reliance Industries in acquiring land for a special economic zone, the company ended up paying $46,000 per acre. "You'll see their lives totally change," says Vivek Tripathi, at the time a sales manager with ICICI Bank who was on hand to help the newly rich farmers set up bank accounts. "They're buying SUVs like biscuits."

Sometimes villagers are savvy enough to band together to get a better deal. More than 120 families living near the city of Pune pooled their 400 acres and created Magarpatta Township & Construction. That company now leases land to developers, who have turned it into an IT park, schools, and hospitals. The value today is $252,000 an acre, or 10 times what it was when the company was formed a decade ago.

A TATA MOTORS PLANT IN WEST BENGAL WOULD HAVE DISPLACED SOME 8,000 PEOPLE WHILE CREATING JUST 1,000 JOBS

The Pune group and those that Reliance dealt with, though, are relatively sophisti-


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Mohanto outside her new home in a Tata resettlement colony

cated farmers on the fringes of India's largest cities. Vedanta Resources, a $6.6 billion aluminum, zinc, and copper producer, has spent five years staring down an indigenous people who inhabit a remote section of Orissa called the Niyamgiri hills. The 8,000 Dongria Kondh still hunt with bows and arrows and worship one of the hills, calling it Niyam Raja, or God of Justice. The Dongria's face-off with Vedanta caught the eye of activists in Britain, who have mounted a vigorous publicity campaign against the company. Bianca Jagger has led protests at Vedanta shareholder meetings in London, while others have lobbied the Church of England to sell its $4 million investment in the company. Troubled by Vedanta's actions, Norway's government investment fund sold its $15 million stake in 2007.

"THERE WAS NOTHING HERE"

The protests, though, only delayed Vedanta in Orissa. Below the Niyamgiri, the company in August finished the first section of a $9 billion plant, which when completed will be the world's biggest aluminum refinery. Touring the facility, Chief Operating Officer Mukesh Kumar can barely contain his pride. "There was nothing here, absolutely nothing," he says. "And in record time we have built this amazing plant."

But Vedanta today isn't making its aluminum using bauxite mined from the Dongria's sacred hills, and instead trucks it in from the other side of India. Before the plant can reach its full potential, the company must get permission from India's environmental watchdog to start mining at the site. After fending off opponents who say the mine will decimate the landscape, the company is likely to get final clearance from Delhi by year-end—though the Indian Supreme Court has ordered Vedanta to hand over 5% of the facility's pretax profits to an environmental group. Today, a half-finished conveyor belt snakes up the slopes from the plant, ready to start feeding on the hilltop's 78 million tons of bauxite.

While the dispute highlights the difficulties of getting land, it also reveals the complexity of the debate. Even as the Dongria Kondh have opposed Vedanta, their cousins who lived at the foot of the Niyamgiri agreed to move in exchange for new houses, a school, and one job per family that pays some $250 a month. "I am not saying we are philanthropists, or that we are going to save the Dongria," says Kumar, the Vedanta plant boss. "But I honestly believe that we will create opportunities here."

Up on the unspoiled hillsides, the clock seems to have stopped ticking centuries ago. During a recent harvest festival, villagers beat drums and carry out ritual slaughter of chickens and water buffalo while a holy man runs over a bed of red-hot coals. But the Dongria are deeply impoverished and often perish by their early 40s from cholera and other preventable diseases. Exhausted by their hardscrabble life and weary of protests against Vedanta, some are now ready to accept the plant and the changes it will bring. "Two years ago, my wife died because there was no road for a doctor to come up here," says Damo Majhi, a 32-year-old Dongria. Had the Vedanta project been built, he muses, she might have been saved. "If there's a road, there is a doctor, there is a school, there is food, then my daughters might not die." | BW |

–With Prashant Gopal in New York

Business Exchange

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Cutting Through Red Tape

Finding land isn't the only hassle faced by companies setting up shop in India. The World Bank's *Doing Business in India* rates 17 cities in areas such as contracts, taxes, and registering property. Ludhiana and Hyderabad get high marks, while Kolkata and Kochi rate poorly.



To view the report, go to **http://bx.businessweek.com/india-business/reference/**



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BETTING BIG ON A BOOM IN NATURAL GAS

By Steve LeVine and Adam Aston
Illustration by Raymond Biesinger

With prices low and the promise of vast new supplies, businesses are making the switch from oil-based fuels and coal

Earlier this year the time came for Lloyd M. Yates, CEO of Progress Energy, to decide how the big Raleigh (N.C.) utility would meet the state's stringent smokestack laws. First he considered the easy solution: installing pollution scrubbers on the utility's old coal-fired plant in Sutton, N.C., at a cost of $330 million. Then his attention turned to natural gas, the price of which had plunged by two-thirds in the previous year. Sure, the recession accounted for some of the slide. But reports were also circulating of massive discoveries of natural gas in the U.S. Moreover, because the fuel emits half the carbon of coal, it seemed safe from the climate legislation being considered in Washington, which could impose steep penalties on emissions.

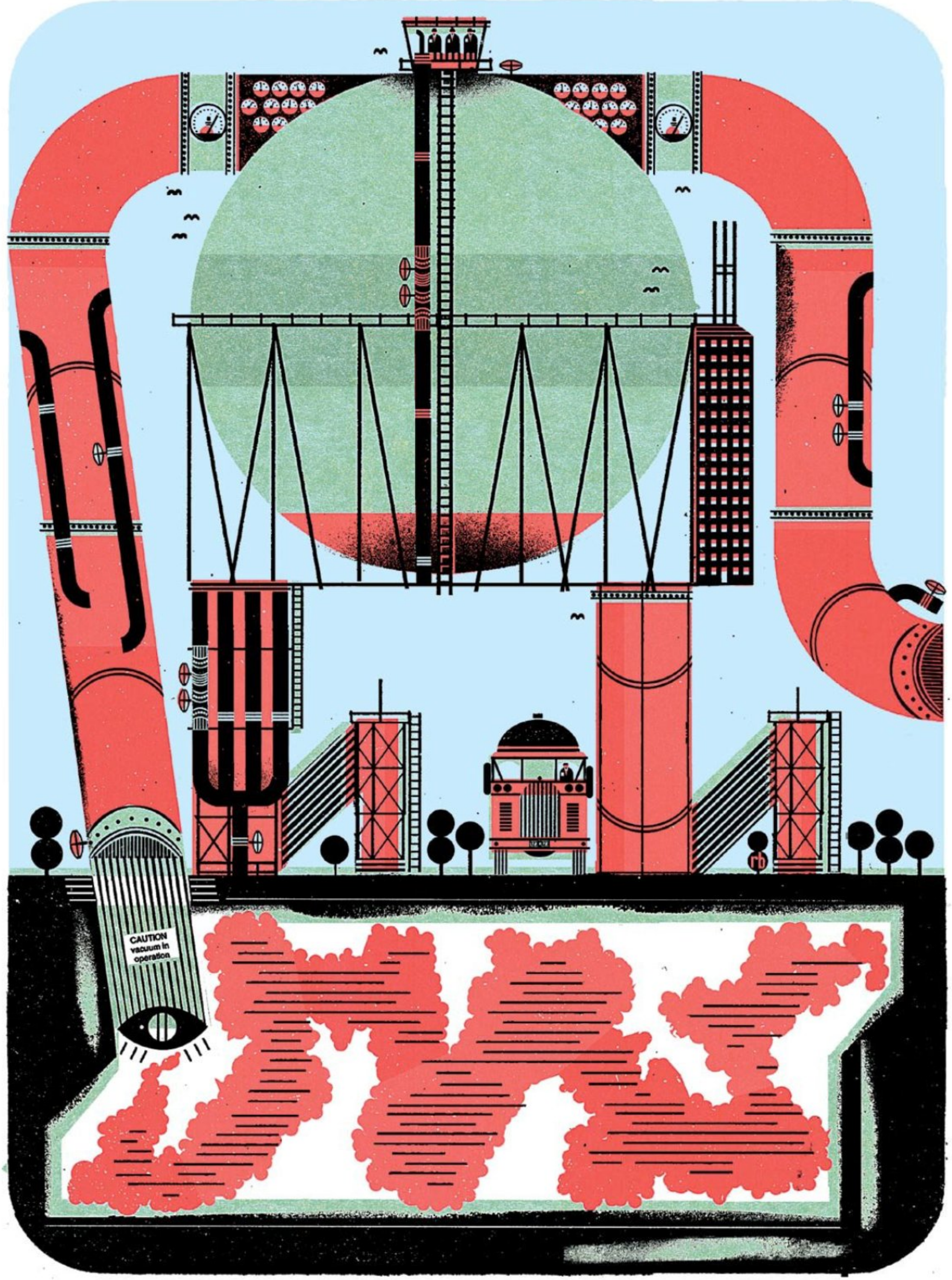
After weighing their options, Yates and his board decided against the scrubbers and opted to upgrade another coal plant to natural gas—a $900 million project. In Yates' calculations, that would satisfy the smokestack law and more than pay for itself over time. "It was like deciding whether to put a catalytic converter on a '52 Chevy," Yates says. "It was: 'When do you buy the new car?' "

The U.S. natural gas industry hopes that as Lloyd Yates goes, so goes the country. In summer 2008 the U.S. and much of the rest of the world were consumed by talk of peak oil and natural gas and fears that high fuel prices would persist forever. Today analysts still worry about the oil supply but far less about natural gas. U.S. gas producers, capitalizing on a technological breakthrough, have in recent years unlocked an enormous volume of natural gas in the shale rock under Colorado, Oklahoma, Pennsylvania, Texas, and other states. According to a July report by the Colorado School of Mines, the U.S. now holds 1,800 trillion cubic feet of natural gas, one third of it in shale, the equivalent of some 320 billion barrels of oil. That's more than Saudi Arabia's 264 billion barrels.

HOW TO PLAY IT 062

Of course, natural gas isn't interchangeable with oil and won't solve America's energy woes by itself. While natural gas can be used to heat homes and power vehicles, it's mostly used, like coal, to generate electricity.

But the supply estimates for natural gas are so vast and the plunge in prices so steep that they're forcing business leaders to rethink their long-term energy strategies—quickly. Utilities are debating whether to retrofit coal plants for gas. Big corporations such as AT&T and UPS are beginning to convert large truck fleets from oil-based gasoline to natural gas. Even renewable-energy players are jumping in: As they try to coax more power from unpredictable wind and solar generators, they're finding that inexpensive natural gas helps keep their output steady.


CAUTION
vacuum in
operation

It's not certain that the gas boom will fulfill its promise. "We don't know if it will be truly awesome or only theoretical in its impact," says David G. Victor, a professor and energy expert at the University of California at San Diego. While natural gas producers say they're sitting on the greatest volumes ever, they also face considerable barriers to getting their commodity to market. Prices are so low that many producers have closed their wells. Most utilities fitted with coal-burning units remain reluctant to invest in natural gas equipment. Critics say the water-intensive shale-drilling process poses risks to nearby drinking water supplies (page 49). And skeptics point to the late 1990s, another era when prices seemed permanently lowered, only to spike a few years later. "Utilities have been burned many times," says Andre Begosso, an energy strategist at Accenture, a consulting firm.

39%

Growth in U.S. natural gas reserves from 2007 to 2009

Data: EIA

Yet the opening up of U.S. shale gas may make the current wave of discoveries different from those of the past. A technique developed in the late 1990s by tiny Mitchell Energy & Development is driving the action. Before hydraulic-fracturing, as the technique is called, gas that was encased in solid shale was untappable. Mitchell and others figured out how to inject the rock with water and chemicals to release the gas molecules. Another recent advance has made it possible for drillers to fan out horizontally, recovering gas from far larger areas than in the past. U.S. natural gas production rose 14% between early 2007 and mid-2008, in large part because of new fields such as the Barnett Shale in Texas.

And the shale boom is only in its infancy. In 2004, John H. Pinkerton of Range Resources drilled the first such well in Appalachia, the Marcellus Shale, a 62 million-acre gas field spanning some 600 miles north to south. Since then Pinkerton has beefed up a one-person Pittsburgh office to 150 geologists, geophysicists, and engineers. Pinkerton says his production has quickly tripled, to some 90 million cubic feet a day. "We expect to double that next year, and again in the following years," he says.

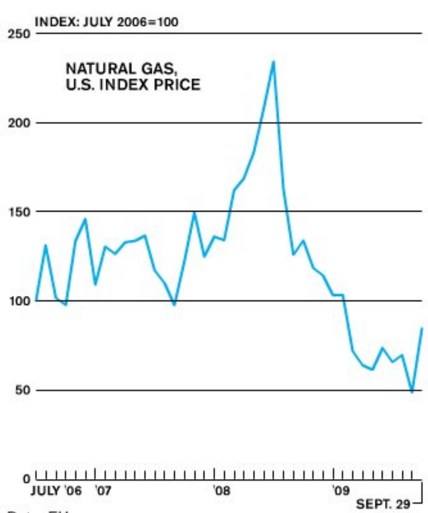
In Raleigh, Progress Energy's Yates made his decision to shift to natural gas in the face of a state requirement to cut the utility's sulfur dioxide emissions in half, to 50,000 tons a year, by 2013. To do so in time, the utility had to act this year. After weighing the options it chose natural gas, in effect betting that prices would stay low for a while. Output at the plant will rise considerably, with a 950-megawatt natural gas unit replacing 397 megawatts of coal-fired capacity. And it will do so while also meeting the sulfur dioxide requirement: It will lower carbon dioxide emissions by 60% and nitrogen oxide by 95%, and will eliminate mercury emissions.

If Washington puts a cap on carbon emissions, Yates will likely face another decision on how to modernize Progress Energy's three other 1950s- and '60s-era coal-fired plants. Yates says natural gas will figure prominently in the calculations, while "we are not even considering coal because of its cost."

A few other utilities are making the shift to gas or considering doing so. Tampa Electric has transformed its coal-fired Gannon Power Station into a natural gas unit at a cost of $750 million. In April, developers of the Highwood Generating Station near Great Falls, Mont., dropped plans to burn coal and chose natural gas for a new plant. Portland (Ore.) General Electric is proposing to build two new natural gas plants.

Most utilities, however, remain on the sidelines. Natural gas prices have been so volatile over the years that executives are unwilling to make a long-term commitment. That's because if they lock in a guaranteed supply at higher prices than today's and prices don't rise to that level, they might have to raise the rates they charge customers. That wouldn't be an easy sell to regulators, who "are not keen on cost-recovery for wrong-

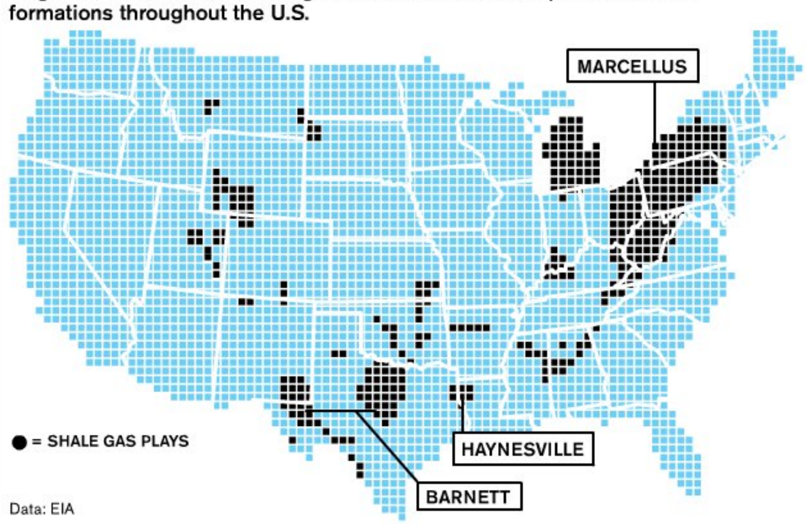
GAS PRICES PLUNGE...



Data: EIA

...AS SUPPLIES EXPAND

Huge new reserves of natural gas have been found deep in shale-rock formations throughout the U.S.



Data: EIA



CHART BY ALBERTO MENA/BW; MAP BY LAUREL DAUNIS-ALLEN/BW



CEO Pinkerton expects Range Resources to double its gas output next year

way bets on supply contracts," says James Owen, spokesman for the Edison Electric Institute, an industry lobbying group.

Oddly enough, natural gas is finding more popularity among utilities that embrace renewable energy. Fears that cheap natural gas might take investment from costlier solar and wind power have proven overblown; instead, utilities are building both. Because gas turbines can vary their output with precision, they complement wind farms and solar fields that generate irregular power flows. The result is a more stable and reliable energy supply.

Florida Power & Light, the nation's largest renewable-energy developer, is building a solar thermal power plant that will be the nation's second largest. The Juno Beach (Fla.) company put its new facility next to an existing gas-fired plant so that when a cloud passes in front of the sun, the gas plant can keep the power flow steady. Public Service Enterprise Group, a major mid-Atlantic utility, is developing gas and renewable projects simultaneously. "The ease of dispatching gas-combustion turbines makes them perfect complements" for wind and solar plants, says PSEG CEO Ralph Izzo.

General Electric has targeted a line of fast-start gas turbines at renewable projects. As part of a $320 million investment, Topeka (Kan.)-based Westar Energy has paired four of those turbines with 300 megawatts' worth of wind capacity spread around the region. It's a wind-rich area, where gusts not only die suddenly but also get too brisk, forcing the turbines to shut down for safety. In either event, gas turbines can kick in to maintain power. Westar committed to build the turbines back in 2006, when gas was double today's price. Now, with prices so low, "they offer an extra benefit, supplying regular power too," says Greg A. Greenwood, a vice-president at Westar.

DAVE SHAFER

Natural gas is also making a small dent in the transportation market. AT&T in March announced that it would be replacing 8,000 service vans with natural-gas-powered vehicles. The 10-year, $350 million upgrade came as part of a $565 million alternative-fuel vehicle initiative started last year. Rising gasoline prices are turning skeptics into believers. From April to July the average price of a gallon of gasoline jumped by 22%, to $2.46, while the price of compressed natural gas for cars rose just 6%, to the equivalent of around $1.73. "When the price of gas rises at the pump by a cent and you're buying about 80 million gallons of fuel a year, it gets pretty expensive," says Jerome Webber, AT&T's vice-president for fleet operations. The company is betting the new vehicles will save it 49 million gallons of gasoline over the next decade. Transportation giant UPS, meanwhile, deployed 300 new natural gas vehicles in February alongside 800 already on the road.

The market for natural gas vehicles is limited by the dearth of fill-up stations in the U.S. Just 1,100 of the country's 162,000 stations sell natural gas, according to Natural Gas Vehicles for America. But that number is growing. Clean Energy, a Seal Beach (Calif.)-based company backed by T. Boone Pickens, has installed 184 natural gas stations in North America and plans to add up to 80 more in the next two years. Utah's Questar Gas has built 20 along that state's I-15 corridor and plans six more over the next 18 months.

Of course, the CEOs of natural gas outfits understand that such inroads don't amount to much compared with the massive reserves still sitting underground. They've descended on Washington in recent months to persuade lawmakers to create incentives for gas use in a climate-change bill moving through Congress. By boosting demand over the long term they hope to strengthen their position vs. Big Coal and Big Oil.

Whether or not they succeed in D.C., the shift away from coal and toward natural gas seems likely to continue, at least for a while, as the price and policy dynamics point in its favor. Says PSEG's Izzo: "We're building gas turbines because... there's no other option in the near term." |BW|

–With Brian Burnsed in Washington

Business Exchange

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Shale Gas: Good or Bad for the Environment?
Cheap natural gas is "the single biggest game changer for climate action in the next two decades," writes Joseph Romm, of the Center for American Progress, on his blog. If the U.S. were to replace half its coal-fired plants with gas, it would cut all the emissions called for in proposed climate legislation by 2020. But such a shift could pollute local water, land, and air. Amy Mall of the Natural Resources Defense Council runs a blog that catalogs the environmental effects of natural gas drilling.

To read both, go to: **bx.businessweek.com/natural-gas-markets/reference/**

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ECONOMICS & POLICY

Health Costs: Steeper Still

Workers will carry a greater share of soaring premiums in 2010, but employers are taking a hit, too

By Catherine Arnst

U.S. businesses struggling to cover their employees' medical needs can expect no relief next year. The cost of insuring employees will rise by 7%, greater even than the 6% increase in 2009, according to a just released survey by management consultant Towers Perrin. That will bring average spending per employee to $10,212, the first time it has hit five digits.

Workers will have it even worse than their employers, due to a combination of premium increases, higher co-pays, and other changes to plans. The new survey of 279 large corporations found that the employee share of health premiums will rise 10% on average, to $2,292, after an 8% increase in 2009. On top of that, employees will have to absorb an additional $200 increase in co-pays and other costs. "Employees are going to feel the impact more keenly at a time when wages are flat or declining," says David Guilmette, a Towers Perrin managing director.

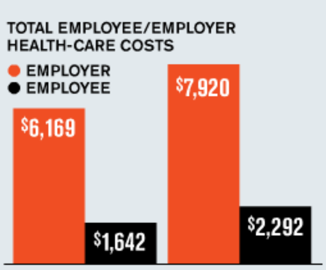
Employers' health-care costs have risen 149% since 2000, which is one reason wages have grown only 37% over the same period. Some two-thirds of insured Americans, 175 million people in total, are covered by private employers. Which explains why so many companies broadly support the health-care reform efforts in Washington.

If Congress fails to act, a bad situation could get much worse, many studies predict. In August the nonprofit Commonwealth Fund estimated that the total premiums for employer-based health insurance will rise 94% by 2020 if current trends continue, to an average of $23,842 per family. Last month the Business Roundtable warned that without reform total health-care costs borne by corporate America will soar 166% over the next 10 years, to nearly $29,000 per employee.

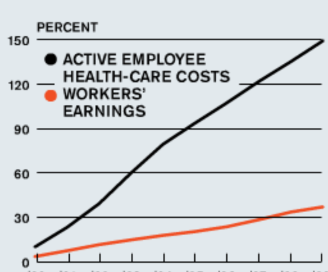
In a Mercer management survey, also released in September, 40% of employers said they would raise employee premium contributions next year, while 39% said they would bump up deductibles and co-pays. Even these increases probably won't be sufficient to avoid collateral damage to benefits. "We know that take-home pay and retirement savings are being sacrificed to maintain health benefits," says Commonwealth Senior Vice-President Cathy Schoen.

SHIFTING THE BURDEN

Health-care outlays continue to climb...



...far outpacing workers' salary gains



Soon, more costs will shift to employees...

$404

EXPECTED AVERAGE INCREASE IN WORKERS' PREMIUMS AND OTHER COSTS IN 2010

...some of whom will receive incentives to stay healthy



Data: Towers Perrin 2010 Health Care Cost Survey of 279 companies

*As identified by Towers Perrin



KEITH NEGLEY

In a separate Towers Perrin survey last summer, 90% of the companies polled said cost containment is their most important health reform goal. Most said they would not absorb additional costs that might result from a reform bill. But companies show no desire to drop health benefits, currently offered by 99% of companies with 200 or more workers. "This is far more than just a medical spend," says Dr. Pamela Hymel, senior corporate medical director at Cisco Systems. "It's about enabling people to stay healthy and be productive."

INVESTING IN WELLNESS

Instead of cutting coverage, some corporations are eyeing ways to intervene in their employees' medical or lifestyle choices to hold down costs. Wellness programs are already common. More businesses are also offering programs to manage chronic diseases, running discount pharmacies and providing free blood screening to assess health risks. Towers Perrin found that the companies it identified as most effective at managing their workers' health needs shaved as much as $1,800 per employee off their health-care costs.

American Financial Group, a Cincinnati insurer with 5,500 employees, has been able to keep cost increases at 2 1/2% each of the past five years, says Scott H. Beeken, assistant vice-president for benefits planning strategy. This year, though, the increase will be higher, due to the rising incidence of chronic diseases such as obesity, diabetes, and asthma. "Chronic illnesses are really where the costs are concentrated. It's a challenge for the whole system," Beeken says.

He notes that outlays have been cut by as much as 20% for employees enrolled in the company's disease-management programs—but only half of those eligible are participating. "The rest don't even return a phone call," says Beeken. "We are really struggling with how to get people engaged."

Cisco thinks the answer to getting people engaged is convenience. A year ago it opened an on-site health clinic in its San Jose office for its 17,000 employees and their dependents in that area. The goal is to make it easier for employees to manage all their health needs in one place. Cisco expects to see savings in two to three years.

The companies in the Towers Perrin survey with the best handle on health care costs say they plan to expand these efforts over the next three years. Among this group, 52% will offer wellness programs in 2012, up from 30% now; 38% will offer disease-management programs, a 20-point jump; and 43% will start disease screening, compared with 24% now. | BW |

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Why High Costs Hurt

A study in the July issue of *Health Services Research* found a direct link between the rapid growth in U.S. health-care costs, job losses, and lower output. Researchers found that, between 1987 and 2005, industries in which most employees receive health insurance showed slower employment and growth compared with those where such benefits are less common. The study was sponsored by the RAND Corp. and the Health & Human Services Dept.

For this and related stories, go to **http://bx.businessweek.com/health-insurance-reform/reference/**

Return of the Mortgage Cramdown?

That's one option being considered as Washington searches for ways to relieve struggling homeowners



PAUL BLOW

By Theo Francis

With foreclosures continuing to climb and midterm elections just a year away, Congress once again is preparing to tackle the mortgage crisis aggressively. High on many a wish list: a renewed push to allow so-called cramdown, which would let bankruptcy judges adjust the terms of home loans to give borrowers relief.

The banking industry hates cramdown (from the idea of cramming deals down lenders' throats), but Democrats argue that earlier efforts to fix the housing mess have not done as well as hoped. Moody's Economy.com estimates that 3.8 million homes will enter foreclosure this year, up 41% from 2008. No surprise, then, that lawmakers are getting an earful. "We have folks calling our office every day," says Senator Jeff Merkley (D-Ore.), who is pressing Treasury to streamline its program to restructure mortgages.

"TRYING TO LIGHT A FIRE"

So Capitol Hill is poring over more ideas. One bill, introduced by Senator Jack Reed (D-R.I.) on Sept. 30 and co-sponsored by Merkley and two other senators, would force lenders to pause before they foreclose and to offer borrowers a break on their mortgage bill if they qualify for help under the Treasury program. Under the same proposed law, states could require mortgage servicers to enter mediation with borrowers before being allowed to foreclose. The bill also would give the states $6.4 billion to help homeowners stay put. "We're really trying to light a fire under the Administration," Merkley says.

Others in the Senate are considering the temporary suspension of home-loan payments or brief monthly mortgage subsidies for unemployed homeowners. House Financial Services Committee Chairman Barney Frank (D-Mass.) is drafting similar legislation.

The Administration is considering new options, too. One would support the broader housing market by extending a homebuyer's tax credit and making it easier for Fannie Mae and Freddie Mac to finance mortgages. Another would fund state housing agencies and independent mortgage banks. A Treasury spokeswoman noted that the Administration's programs have done more than previous efforts but said it "aggressively continues to build on our progress to date."

Many congressional Democrats think mortgage lenders need to feel the lash before they'll speed up mortgage workouts. Those critics, led by Senator Richard J. Durbin (D-Ill.), figure banks and mortgage servicers will do their best not to cut principal or interest rates on a mortgage. Lenders want to avoid, or at least delay, the loss they take from lowering what homeowners must pay, critics say. And despite an Administration plan that gives subsidies to mortgage servicers who agree to rework loans, many believe the service firms still gain too much from the fees they collect in foreclosure to bother

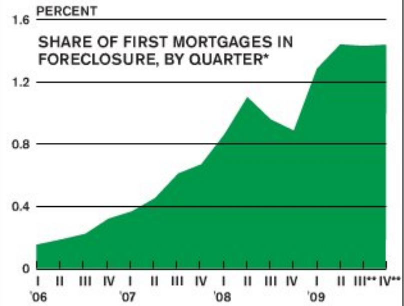
working out a loan.

Durbin and other lawmakers are calling on Democrats to support what is seen as the party's nuclear option: cramdown. The proposal, which sailed through the House last spring, only to stall in the Senate on a 45-51 vote, authorizes bankruptcy courts to adjust mortgages. If Durbin's bill were to pass, a judge could reduce principal or interest rates on home loans and stretch out mortgage payments—something bankruptcy courts can do already with virtually every other kind of debt.

Supporters say cramdown would free homeowners from debt they can't afford while prodding lenders to cut deals before reaching the courthouse. A bankruptcy-court solution would also cost taxpayers little or nothing. Detractors argue cramdown would spook the mortgage market, driving up borrowing costs and making loans harder to get.

Undeterred, Durbin, the second-ranking Senate Democrat, is willing to attach a cramdown provision to any convenient bill if it won't get a hearing on its own. The proposal "will always be part of the conversation, if for nothing else than to scare the [daylights] out of everyone," says one senior Senate aide.

MORE FORECLOSURES



*Seasonally Adjusted **Projected
Data: Mortgage Bankers Assn.'s National Delinquency Survey, Moody's Economy.com

CHART BY JOE RHAMES/BW

The financial industry, which used major muscle to kill the provision last spring, is arming for the fight, too. "The vote in the Senate was so overwhelmingly close, we're always worried," says one lobbyist. The big banks are leaning on community banks for help: These institutions were largely innocent of the worst excesses of the crisis and tend to be viewed much more favorably on Capitol Hill. "We are kind of the white hat," says a lobbyist for smaller financial institutions. "You'll see a lot of the industry try to hide behind us."

Given the industry's stance, supporters of cramdown say a forceful campaign by the White House would help. President Barack Obama supported it during the campaign and soon after his election, while his chief economics adviser Lawrence H. Summers wrote columns in favor of the proposal last year. But congressional sources say the Administration did little to push for passage of the bill last spring—possibly because Obama was reluctant to place further stress on already fragile banks. Now one Treasury official says the department has "no immediate plans" to revive the measure. Yet even without stronger White House support, Durbin might attract enough senators to embrace the bill if foreclosures continue to surge. |BW|

—With Jane Sasseen in Washington



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Test-Drives In the C-Suite

Companies are turning to tryouts to avoid hiring the wrong executive

By Michelle Conlin

At one time or another all executives have experienced that special horror—the moment when they realize they've hired the wrong person. For Justin Moore, the revelation came during his chief financial officer's first week on the job. As Moore, CEO of Axcient, a data storage company in Mountain View, Calif., was scrawling out scenarios at the whiteboard, he started to feel as if he were pulling the new guy up a hill. "I was constantly having to lead him into a high-level discussion and say, 'Come on, get high-level again. Let's think more strategy here.' "

Moore had an out. Like a number of executives, he has scotched standard operating procedure in favor of a new hiring strategy: trying before buying. Once Moore finds a potential candidate, he auditions him or her before making a permanent offer. Sometimes tryouts last weeks, sometimes months. Why get married after only a few dates? "It's foolish of any of us to think our interview skills are so great we can predict how well someone is going to work in terms of the dynamics of a team," says Moore.

With all the Grade A talent on the street these days, bosses often have the leverage to put potential recruits through their paces. And why not?



Interviews alone are inadequate to gauge suitability, says Axcient CEO Moore

After all, 40% of executives hired from the outside last only 18 months, says Heidrick & Struggles International CEO L. Kevin Kelly. In Europe and Asia, "interim executives" have long been popular. Now the practice is creeping into the American C-suite, too.

It remains to be seen whether so-called try-buys will proliferate once the labor market recovers. But for now it suits the times. Executives don't want to commit to big fixed costs. Job hunters don't want to change cities or update their LinkedIn statuses before they know a job is a sure thing. In an acutely risk-averse environment, try-buys mitigate the risk on both sides. No contracts. No severance. No drama.

In an acutely risk-averse environment, "try-buys" mitigate the risk on both sides. No contracts. No severance. No drama.

Companies are increasingly turning to "leadership on demand" services. Last summer, Pauline Brown, a managing director at the Carlyle Group, a private equity firm, was in a bind. One of Carlyle's consumer goods companies was suddenly without a CEO. Carlyle hired a search firm to find a replacement. But because the big headhunters almost always focus on candidates who already have jobs, those hunts typically take months.

So as a hedge, Brown decided to experiment. She phoned the Business Talent Group, an agency in Los Angeles with a gold-plated roster of 1,000 executives with Ivy League MBAs and experience at such outfits as McKinsey. With clients that include Fox Mobile, Healthways, Maveron, and Pinkberry, BTG is at the forefront of creating a spot market for executive talent. BTG offered Brown a roster of candidates who could start within two weeks. "I was basically blown away by the caliber of people they presented," says Brown. "They were on a par with or better than the people we were meeting in our more standard search." In the end the temporary candidate beat out all the ones the traditional search firm eventually supplied and is now the permanent CEO. "I wouldn't hesitate about trying this again," Brown says.

BTG is onto something. Heidrick & Struggles itself recently launched a new business called the Chief Advisor Network. It too functions as a talent agency for C-suiters who can be placed on quick notice. "We are in this moment when organizational design is shifting," says managing partner Lauren Doliva. "That means more try before you buy." |BW|

TIMOTHY ARCHIBALD

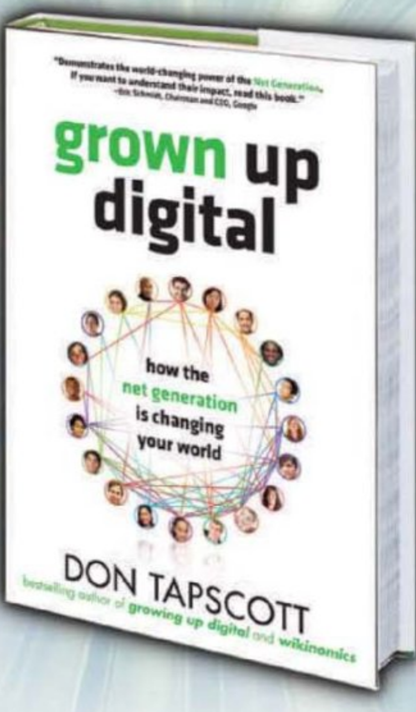
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Gunning for an Elephant In Silicon Valley

Tiny Arista, started by a Sun co-founder, is challenging Cisco with superfast networking gear

By Peter Burrows

If you don't envy Andreas Bechtolsheim, you may not know enough about him. Even by the standards of Silicon Valley hotshots, his combination of talent and luck is rare. In 1982 the brainy young engineer co-founded Sun Microsystems and helped usher in a new era of computing by dreaming up a workstation that was cheaper and more versatile than the minicomputers popular with companies at the time. Then in 1998, at a friend's house in Palo Alto, Bechtolsheim had the good fortune to meet two young Stanford University grad students working on a new search engine. He wrote the pair a check for $100,000 on the spot, and Larry Page and Sergey Brin proceeded to turn his initial stake into more than $1 billion in Google stock.

Now the 54-year-old has an audacious new goal: taking on Cisco Systems. Although Cisco is the dominant provider of the networking equipment at the heart of the Internet, Bechtolsheim thinks his tiny Arista Networks has an edge in the fastest-growing part of the market: blazing-fast gear for the data centers where more and more computing is done. If he's right, Arista could undercut Cisco in a critical business, complicating the giant's efforts to hit CEO John Chambers' aggressive growth goals. "We're just a fly in the ointment to Cisco today," says Bechtolsheim. "But it's very hard for large companies to change their fundamental business models."

Bechtolsheim has been called the Steve Jobs of corporate computing

He claims an edge in cost and performance. Arista's switches, computers that direct traffic around the Net, are less than half the price of comparable Cisco products. Lane Patterson, chief technology officer of data center company Equinix, says Arista's equipment can be one fifth the cost, "a phenomenally compelling price." Its gear also runs on cutting-edge software that analysts say has advantages over Cisco's 20-year-old software, IOS, which is as prevalent in networking as Microsoft's Windows is in personal computing. Arista's software has the potential to run more kinds of programs and won't crash if one gets a bug.

Cisco isn't showing any sign of vulnerability. Its hold on the networking market is so complete it's branching out into dozens of new markets, from video to wireless technology. Competition is increasingly from tech giants, particularly Hewlett-Packard. Cisco declined to comment on Arista but points out that Cisco has 1,000 customers for its data-center products, while Arista claims 130.

Still, Arista is getting traction. The company has a broad clientele only two years after introducing its



ERIC MILLETTE

Andreas Bechtolsheim

Born Sept. 30, 1955

Hometown Ammersee, Germany

Claim to Fame Known as a master computer designer since designing a PC-like "workstation" as a Stanford student. He and three others formed Sun Microsystems to sell the machine.

Cisco Connection Licensed computer designs to Cisco's founders while at Stanford, then sold Cisco a startup in 1996 for $220 million.

Midas Touch
His $100,000 investment in Google in 1998 is worth more than $1 billion.

first product. A third of its customers are big Wall Street firms looking for faster computing systems and speedier execution of trades. Bechtolsheim also recruited a heavyweight to lead the company, Jayshree Ullal, former architect of Cisco's own data-center effort. "[Arista] is doing very well," says Pacific Crest Securities analyst Brent Bracelin. "Clearly there's a strong appetite for alternatives to Cisco."

SELLING HIS STARTUPS

Bechtolsheim has long been ahead of his time. He grew up on a farm in Germany and earned $100,000 at age 16 by writing software for a local tech firm. He came to the U.S. on a Fulbright Scholarship but dropped out of a doctoral program at Stanford University to help found Sun. After leaving Sun in 1995, he kept spotting opportunities to do what tech leaders were doing, only cheaper or better. He sold one startup to Cisco for $220 million and another to Sun for $91 million. "Andy is to corporate computing what Steve Jobs is to consumer computing," says Sun co-founder and Chairman Scott G. McNealy.

Bechtolsheim sees opportunity in networking in part because of Cisco's dominance. The company specializes in reliable gear and strong customer support, charging premium prices that help garner 65% margins. That's a winning formula with Cisco's bread-and-butter customers—conservative corporate buyers most concerned with keeping their networks up and running. But for companies building big data centers—Wall Street firms and Net giants such as Google—slashing a few milliseconds off a stock trade or search query is more valuable than kid-glove support. "We are totally convinced we have a home run on our hands," says Bechtolsheim.

That is, unless he decides to sell out again. Already, there's talk IBM or HP might try to buy Arista. Bechtolsheim insists that's not his plan. Arista is much further along than his previous startups, and he's cranking up his sales effort for a possible initial public offering. While he admires Cisco, Bechtolsheim says tech industry history is full of fallen giants. "It's strange how none of the big companies were the winners in the next era," he says. | BW |



Ito says bike sales in the developing world will help boost profits

MAKOTO ISHIDA

STRATEGY & COMPETITION

What Put Honda In the Passing Lane

Frugal management and a focus on gas-sippers have served the Japanese carmaker well in the recession

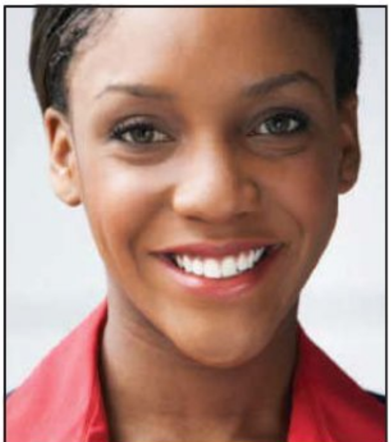
By Ian Rowley



TOKYO

Takanobu Ito is used to making do on a budget. For years he commuted to work on his 250cc Honda Baja motorbike, eschewing the comforts of even an Accord or Civic. Today, although he became Honda Motor's CEO in June, he works from a plain wooden desk in a room with nearly a dozen other executives. Many management meetings are held nearby at a small round table with four stools.

That kind of frugality has helped Ito—and Honda—successfully negotiate the downturn. For the fiscal year ended in March, Honda made a profit of $1.5 billion, while Toyota Motor lost $4.9 billion and Nissan Motor $2.6 billion. This year, Honda is predicting earnings of some $600 million. Toyota expects to lose $5 billion and Nissan nearly $2 billion. "Sales will continue to be slow, but compared with the others



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we are perhaps better off," says Ito.

It helps that Honda has the right product mix for the times. With its lineup of gas-sippers, it has benefited from U.S. drivers' abandonment of big SUVs in favor of compacts. And Honda is the world's No.1 motorcycle maker. Bike sales are likely to account for half of operating profit this year as buyers in developing countries get mobile on two wheels.

NO BIG PICKUPS

But Honda's recent strength is also due to its culture. The company has long emphasized quick thinking, conservative investments, and a level-headed assessment of its own capabilities, industry watchers say. "The beauty of Honda is they are willing to hear the painful reality," says Tatsuo Yoshida, an analyst at UBS in Tokyo.

Honda's dearth of large vehicles, for instance, is no accident. Earlier this decade executives bucked conventional wisdom when they chose not to follow Toyota and Nissan in building big pickups. "We discussed [developing a V8 engine] several times, but we decided to be prudent," says Ito, 56.

Instead, Honda boosted profits by doing what it does best: building small and midsize vehicles. While bigger cars typically make more money, Honda finds economies by concentrating on four key models—the Fit compact, Civic and Accord sedans, and the CR-V small SUV—in huge volumes. Worldwide, each sells more than 500,000 annually, and together they account for more than three-quarters of unit sales.

Another differentiating characteristic is that Honda is relatively unhierarchical and forgoes many of the trappings of corporate success. Most top executives, including Ito, are engineers and seem more energized talking about technology than discussing finance. While Ito has ditched his motorcycle for a chauffeur-driven Legend sedan (the home-market version of the Acura RL), Honda says it's only for security. And virtually everyone refers to the boss as *Ito-san*, rather than the more formal *Ito-shacho* ("President Ito"). "The thing about Honda is their pragmatism—it's one of the reasons they don't lose money," says Andrew Phillips at KBC Securities in Tokyo.

Although Ito concedes Honda was slower than some rivals to tackle the global downturn, he says it was because the company initially fared reasonably well. "Once we started to consider what we had to do," he says, "we were quick in the decision-making process." Honda delayed construction of two factories in Japan and postponed expansion of plants in India and Turkey. A plan to launch Acura in Japan in 2010 was axed, as was a new sports car, a project Ito had once overseen himself. In January all Honda directors took a 10% pay cut and saw bonuses slashed.

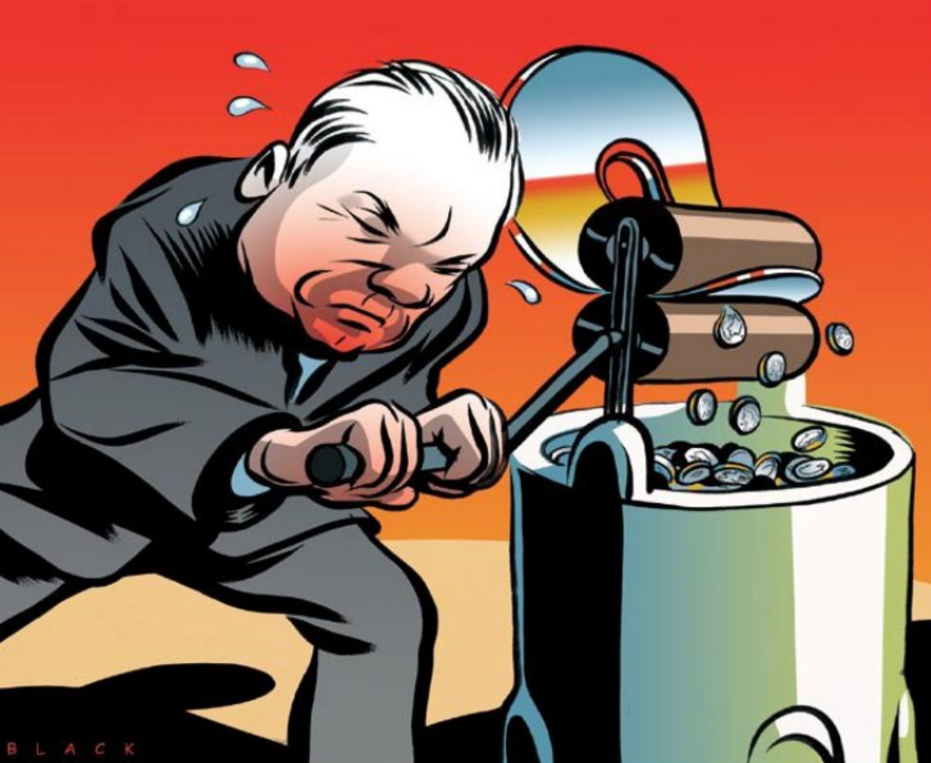
As the former chief of Honda's racing programs, Ito says the hardest move was pulling out of the Formula One circuit in December. He worried the change "might hurt the motivation of Honda people." But quitting the sport saves some $500 million a year. "I have no regrets whatsoever," Ito says.

$600 MILLION Honda's projected profit this fiscal year, vs. losses of $5 billion at Toyota and $1.9 billion for Nissan

Data: Company reports

Ito must now steer the company through a period of depressed sales while readying it for a recovery. One hurdle is the strengthening yen. At its current level of 89 to the dollar, profitable exports from Japan are difficult, although Honda is better off than Nissan and Toyota because its U.S. factories make 80% of the cars it sells there.

Some critics complain that in its frugality, Honda has abandoned flashy models such as the S2000 roadster. The CR-Z, a new sporty hybrid due out in 2010, may appease enthusiasts, but Ito says he won't add zippier cars unless they are environmentally sound. "We want to offer consumers fun-to-drive vehicles," he says. "But gas-guzzlers are not something we want to do." | BW |



STRATEGY & COMPETITION

Squeezing Every Dime from DVDs

With consumers flocking to low-cost Netflix and Redbox, Hollywood wants a bigger share of the profits

By Ronald Grover and Tom Lowry

With frugal consumers renting rather than buying DVDs, Hollywood's $14.5 billion cash cow is getting thinner by the month. And even when the economy recovers and people feel flush again, it seems clear that DVDs will not be high on shopping lists. "The days when you [could] get anyone who wants to see a movie to pay $15 at a Blockbuster, Best Buy, or Wal-Mart are in significant decline," former News Corp. President Peter Chernin told a recent University of Southern California roundtable. "And you're going to see [DVD sales] continue to decline."

It is a measure of Hollywood's desperation that the studios, which rarely agree on anything, are closing ranks to shore up the business. This past summer, Sony, Paramount, and Fox discussed combining back-office and distribution operations as a way of cutting costs and boosting DVD margins. Those talks have since bogged down because hoped-for savings might not materialize quickly enough.

SHARE THE WEALTH?

Meanwhile, some of the largest studios are looking to squeeze more money from Netflix, the fast-growing online behemoth that revolutionized the DVD rental business. Jeffrey L. Bewkes, CEO of Warner Bros.' parent company, Time Warner, told an industry conference in mid-September that his studio wanted "better economics" from its Netflix deal. Time Warner, according to knowledgeable industry sources, is pressuring Netflix to rewrite its agreement either to share more of its subscription revenues or to get DVDs from the studios weeks after Wal-Mart and other retailers get them. A Netflix spokesman says only that it "continues to discuss the changing market" with the studios.

Another player feeling the hot breath of Hollywood is Redbox, the fast-growing upstart whose $1 DVD rental kiosks are in supermarkets across the U.S. In a bid to protect DVD sales, Warner, Universal, and Fox have threatened to withhold titles from Redbox unless it agrees to several restrictions. According to a lawsuit Redbox filed against Universal, they include limiting the number of titles rented in each machine, sharing rental fees, and waiting 45 days after a film has been in stores before renting it. "We think there is a place for very low-priced rentals, but obviously not in the middle of when we are trying to sell higher-priced [products]," said Bewkes at the same conference.

Most studios argue that DVD sales will come back when the economy recovers. But even as the studios take defensive steps against cheap rentals, they're looking at a future without DVDs. Warner recently made two new releases available for rent to a small number of Atlanta cable subscribers four days before the DVDs were set to appear in stores. Warner is waiting to see if making the films available on demand would prompt folks to visit their local Wal-Mart and buy the disk. Fox recently offered a three-disk package of *X-Men Origins: Wolverine* for $26.99 that included a Blu-ray disk, a traditional DVD, and another one that can be stored on a computer hard drive.

After toying with online distribution for years, Hollywood finally seems to be rushing the Net as well. Walt Disney may launch an online subscription channel featuring some of its older family classics. And by Christmas, say industry insiders, Google's giant YouTube video service could start renting movies from most of the studios. "They've been practicing some of these dance steps for a long time," says Lazard Capital Markets analyst Barton Crockett. "It's time they hit the dance floor." | BW |

JACK BLACK

Toys 'R' Us Gets Wound Up Again

Earnings are higher, the retailer is making acquisitions, and an IPO is expected early next year



Looking forward to the holidays at Toys "R" Us in the Bronx; CEO Storch (below)

(TOP) CHRISTOPHER LANE; (BOTTOM) PETER YANG

By Emily Thornton

When a trio of private equity buyers snapped up Toys "R" Us in 2005, many predicted the retailer wouldn't survive. With cutthroat competition in the toy world, some even suspected Kohlberg Kravis Roberts, Bain Capital Partners, and Vornado Realty Trust would convert a number of store locations into condominiums. Instead, Toys "R" Us has expanded its revenues by billions of dollars and is likely to file for an initial public offering in early 2010, people close to the company say.



The turnaround underscores the success of CEO Gerald L. Storch's strategy of integrating baby products with toys while ramping up promotions and exclusive products. Now the world's largest specialty toy retailer is out to build market share. "We have the largest assortment of every product at every price point," says Storch. He is rolling out almost 350 temporary Holiday Express stores across the country in the coming weeks, which will add 1 million square feet of retail space.

While Toys "R" Us is entering the holiday season with more financial strength, having doubled year-over-year earnings, to $27 million in the second quarter, the battle for consumer dollars will be fierce. Wal-Mart Stores is offering more than 100 toys at $10—up from just 10 last year. (Storch counters that his store has 6,000 toys under $10.) Target and Kmart are also beefing up holiday specials. "It's going to be competitive," says Sean McGowan, a toy analyst at Needham. But he predicts that Toys "R" Us will finish the year with $750 million in operating earnings, up from $621 million in 2008.

MORE SELECTION, WIDER REACH

One source of optimism is Storch's choice to compete more on selection and reach than on price. Those efforts to differentiate itself from mass-market retailers, along with a series of recent acquisitions, have helped Toys "R" Us to increase its share of U.S. toy sales. Storch bought eToys.com, Toys.com, and babyuniverse.com over the past year, while also snapping up toy stalwarts FAO Schwarz and KB Toys.

He is extending the retailer's Internet presence and trying to position the traditionally high-end FAO Schwarz as a place to create trends. Storch has also increased the shelf space devoted to exclusive, higher-margin products, such as a $119.99 private-label remote-control toy all-terrain vehicle. When he took over in 2006, Storch reversed plans to spin off Babies "R" Us in favor of integrating its operations with the toy stores.

While Storch won't comment on any plans to go public, industry analysts say the move makes sense. "It's logical to assume the investors in Toys "R" Us want to see a return after investing for five years in the business," says Needham's McGowan. The investment community is enthusiastic about the company, with its strong balance sheet and surprisingly resilient earnings amid the recession.

The key factor in the timing of a public offer will be how Toys "R" Us performs in coming weeks. The fourth quarter typically makes up almost 40% of U.S. sales, and analysts are divided on the outlook for consumer spending. Storch's binge on temporary stores gives him more reach but also risks cutting into profits. Storch is optimistic. "Christmas will come," he says, arguing that few will skimp on gifts for the kids. "We sell toy cars, not real cars, and they don't need financing." |BW|

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MONEY REPORT

A DIVIDEND FOCUS

On Oct. 1, Standard & Poor's said just 191 of 7,000 companies reporting dividends raised payouts in the third quarter. That marks the worst quarter in history for dividend hikes. The good news: Dividends may have hit bottom. Managers are finding dividend-paying stocks they like in retail, pharmaceuticals, consumer staples, and tech. ¶ Don Taylor of the Franklin Rising Dividends Fund looks for companies he thinks will continue to pay—and increase—dividends, rather than those with fat yields. He favors Family Dollar Stores, which yields 2%, and Wal-Mart Stores, which pays 2.2%. Charles Carlson of the *DRIP Investor* newsletter prefers blue chips Johnson & Johnson (3.3% yield) and IBM (1.8%). IBM is also a pick of Rick Helm of Cohen & Steers Dividend Value Fund, as is Intel, which yields 3%, Qualcomm, which pays 1.6%, and Oracle, which initiated a dividend this year equal to 1%. "The idea that tech shouldn't pay a dividend is passé," he says. *–David Bogoslaw and Amy Feldman*

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Number of companies—out of 7,000 reporting dividends—that hiked payouts in the third quarter

Data: Standard & Poor's

EMERGING MARKETS

BRAZIL'S OLYMPIC JUMP

Brazil's Bovespa stock market index has climbed 4% since Oct. 2, when the International Olympic Committee named Rio de Janeiro as host city of the 2016 Summer Games. Investors, eager to capitalize on Brazil's plans to spend $11 billion on infrastructure, pushed up shares of steelmaker Gerdau and mining company Vale—which together make up almost a fifth of the index—9% and 4%, respectively. Morningstar strategist Allan Nichols warns: "Brazil is not a cheap country anymore." So far this year the Bovespa has returned 67%, vs. 25% for the MSCI World Index. Still, its economy is projected to grow 4% a year in 2010 and 2011.

Those willing to accept more risk than that of a broad emerging-markets fund can buy iShares' MSCI Brazil Index ETF. But it's being outpaced by the yet riskier Market Vectors Brazil Small-Cap ETF, launched in May. It has a 23-percentage-point edge.
–Tara Kalwarski

FIXED INCOME

YIELD PLAYS

As of Sept. 30 money market mutual fund assets were down 12.5% from their Jan. 14 high. Still, that's $3.4 trillion in accounts paying ultralow yields: 0.05% is typical. Elizabeth Fell, fixed-income strategist at Barclays Wealth in the Americas, expects yields to stay low. She suggests shifting some cash into higher-yielding, short-maturity "supranational" debt issued by government-related entities such as the European Investment Bank. Its AAA-rated debt maturing in 2011 pays 1.15%, vs. 0.28% on comparable U.S. Treasuries.

Another option: short-term U.S. agency debt from Fannie Mae, Freddie Mac, and the Tennessee Valley Authority. Yields also top Treasuries. Supranational and agency debt "offer a great middle ground" between low-returning government debt and higher-yielding, riskier corporate and municipal debt, Fell says. *–Lauren Young*



Brazilians celebrate Rio de Janeiro's selection to host the 2016 Games

ANDRE PENNER/AP PHOTO

BETTING BIG ON A BOOM IN NATURAL GAS

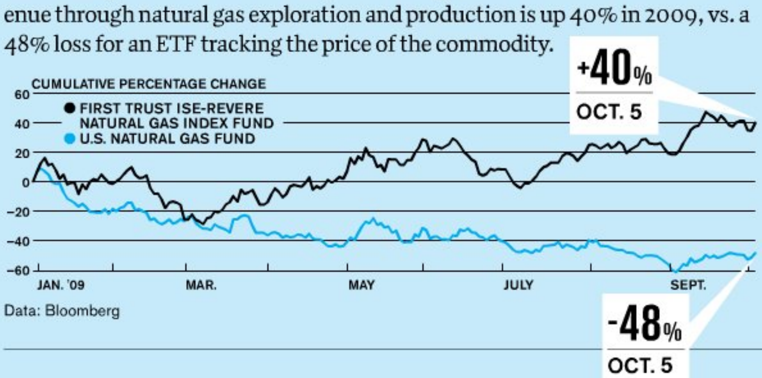
(FROM PAGE 046)

By Tara Kalwarski

Natural gas had quite a rally in September, rising almost 25%, to $4.99 per million BTUs. Still, the beleaguered commodity is a shadow of its former self: It peaked above $12 in July 2008. As clean energy becomes increasingly mandated in the U.S., many think natural gas is a good long-term investment play.

COMPANIES VS. COMMODITY

An exchange-traded fund of companies that generate the bulk of their revenue through natural gas exploration and production is up 40% in 2009, vs. a 48% loss for an ETF tracking the price of the commodity.



Data: Bloomberg

PIPELINE PICKS

Because natural gas is hard to move, there can be big fluctuations in inventories of it, which ultimately affect pricing. Companies that build pipelines could benefit from increased infrastructure spending.

COMPANY/TICKER	SHARE PRICE	YEAR-TO-DATE RETURN
Enbridge Energy Partners/EEP	$45.27	92%
Energy Transfer Equity/ETE	27.71	83
Enterprise Products Partners/EPD	28.27	45
El Paso/EP	9.91	29
Spectra Energy/SE	18.90	26
Kinder Morgan Energy Partners/KMP	54.10	26
Williams Cos./WMB	17.65	25
Enbridge/ENB	38.34	21
TransCanada/TRP	30.89	18

*As of Oct. 5 Data: Capital IQ

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ENERGY FUND OPTIONS

Fidelity offers a mutual fund focused solely on natural gas. But because the commodity is highly volatile, holding a diversified basket of energy stocks is a lot safer.

FUND/TICKER	EXPENSE RATIO	MINIMUM INVESTMENT	TOTAL RETURN* YEAR TO DATE	TOTAL RETURN* FIVE YEAR	COMMENT
Fidelity Select Natural Gas/ FSNGX	0.85%	$2,500	47%	8%	When the natural gas outlook is bullish, this fund loads up on companies that are sensitive to price. When bearish, it buys pipeline and utility companies.
Vanguard Energy/VGENX	0.28	25,000	26	13	This $11 billion fund owns more big energy stocks than most category peers, which protects the portfolio from wild fluctuations in commodity prices.
BlackRock Energy & Resources/ SSGRX	1.25	1,000	52	11	The managers of this fund take risky bets on small-cap energy stocks, but it has paid off: The fund has gained an average 20% a year over the past 10 years.

*As of Oct. 5; multiyear returns are annualized Data: Morningstar

CHART BY DAVID FOSTER

MUTUAL FUNDS

FINANCIALS: WHAT'S AHEAD

Financial-services stocks have come roaring back since their collapse last fall. Are the gains sustainable? For insight on smart ways to play such stocks now, Personal Finance editor Lauren Young spoke with Anton Schutz, manager of the top-ranked Burnham Financial Services Fund, which delivered an annualized gain of 14.3% over the past decade.

What's your outlook on interest rates, and how does that feed into your stock selection?
The Fed will talk about raising rates but isn't going to do it anytime soon. This is too fragile a recovery to take away the punch bowl.

A year ago, I owned a lot of companies tied to the mortgage market, particularly real estate investment trusts such as American Capital Agency. These companies got a lift as the Federal Reserve aggressively cut rates. The easy money has been made there. Now they're caught in a no man's land as rates bottom out. It's an area I'm avoiding.

Who benefits in a low-rate environment?
I like banks because they're getting core deposit inflows from saving, checking, and money-market accounts for the first time in decades, instead of noncore deposits such as certificates of deposit. Core accounts cost banks very little to operate. Until recently banks were in an interest rate war. Weaker banks gathered the bulk of deposits by offering higher yields on certificates of deposit. That forced other banks to match those rates, cutting into profits.

I'm also eyeing banks that gain market share by rolling up troubled rivals. A good example is BB&T's purchase of Colonial BancGroup in August. BB&T bought most of Colonial's assets from the Federal Deposit Insurance Corp. in a deal that could boost earnings by as much as 50¢ a share. The FDIC agreed to shoulder about half of Colonial's losses.



ILLUSTRATION BY ANDY FRIEDMAN

My portfolio is full of smaller banks that I expect will work out similar kinds of deals with the FDIC. One is 1st United Bank, which had a $40 million market capitalization but just raised $70 million. That's how confident the market is in funding stronger banks.

Some big insurers are among your top holdings. Who will be the winners there?
I expect the winners to be the stronger companies, even though the winners in the equity markets lately have been companies that took money from the government to stay afloat. Credit quality still matters a lot. Take MetLife, the nation's largest life insurance company. Even after $1.4 billion in credit losses, the average bond in its portfolio is rated single-A. By comparison, its competitor Torchmark owns lower-rated debt.

In property and casualty, Travelers is boring, and boring is still good. Property-and-casualty prices have stayed stable because there's too much capital in the industry—we haven't had massive hurricanes or other disasters that deplete that capital safety net. American International Group is cutting prices to retain business, but they're grasping at straws because consumers want policies from companies that aren't being propped up by the government.

Travelers and MetLife have a chance to acquire weaker AIG units. Both stocks stand to gain 10% to 20% with the right acquisition.

Will third-quarter earnings for the sector mirror the second quarter, when companies beat earnings estimates but revenues lagged?
The third quarter is going to be different because you have a lot of noncash events going on. Companies that reported unrealized losses in the past will now have unrealized gains. There is going to be a huge uptick in the value of corporate debt, and investors will see those gains reflected in stock prices. |BW|

INSURANCE

IF COBRA IS OUT OF REACH

By Aaron Pressman



ILLUSTRATION BY JESSE LEFKOWITZ

In February the government gave people who lost their jobs in 2009 a big helping hand, agreeing to pay a portion of their COBRA health insurance premium. As part of the stimulus package, Washington is paying 65% of the cost for nine months under the program that lets people keep their health insurance when they leave a job. But eligibility for the subsidy expires at yearend, so those laid off in 2010 will be back to paying the entire cost of their COBRA policies unless Congress acts again.

Typically, employees pay about one-third or less of the cost of health-insurance premiums. So the price of COBRA, which covers the entire premium plus a 2% administrative fee, can be a shocker. Before the subsidy, relatively few people opted for it. A survey by benefits consulting firm Hewitt Associates found only 19% of those eligible for COBRA from September 2008 through February 2009 paid for the coverage, vs. 38% opting for it over the four months, after the subsidy took effect. The cost for the average worker fell from $8,800 to about $3,000 annually with the subsidy, the survey found. The subsidy applies only to people who lose their jobs involuntarily.

Once the subsidy expires, COBRA may not be the smartest or most affordable option. "The subsidy put the cost of COBRA on par with the cost of employer-provided coverage," says Karen Frost, head of the health and welfare outsourcing business at Hewitt. "Historically, it has been more of a last resort."

There are numerous COBRA alternatives. Health-insurance offerings vary greatly by state, since they are mainly regulated at the state level. Careful shopping is required to determine which options are included in a policy if they are not mandated by state rules. And consumer advocates warn that some options, known as limited or fixed indemnity policies, don't offer good value.



Data: Hewitt Associates survey

The first step after losing a job is to evaluate the COBRA plan offered by your former employer. You have 60 days to decide whether to take it. Not all health-related benefits are covered under COBRA or the new subsidy program. The U.S. Labor Dept. has set up a Web site explaining in detail how the subsidy program works at dol.gov/ebsa/cobra.html.

Departing employees who had high-deductible plans combined with Health Reimbursement Arrangements face an added layer of complexity. The HRA is a set amount of money that can be used to cover deductibles or other health-care expenses not covered by the high-deductible policy. Unused money is usually rolled over to the next year. Under COBRA, a former employee would pay a premium for the high-deductible plan and another for the HRA, with both reduced by the 65% subsidy.

If, once the subsidy expires, COBRA is too pricey, state-government-run plans or comprehensive individual plans may be better options. Government-run plans are offered by most states; eligibility requirements vary widely. In Massachusetts, for example, a family of four with an income under $66,156 can opt for the state's Commonwealth Care plan. The premium for the lowest priced of six plan providers is $116 per adult per month. There are also co-pays.



Dozens of insurance companies sell individual plans, usually through a broker or agent. Although some general insurance agencies sell health plans, specialized health brokers may know more about the complexities of particular policies. Healthy people should be able to find an individual policy with good coverage at substantially lower cost than their former employer's COBRA plan, says Jon Moss, founder of Chattanooga-based Moss Benefits Group, who helps small businesses and individuals buy health insurance.

With varying state laws and without the bargaining power of employers, shopping for individual plans can seem a bit like the Wild West, says Eliza Bangit, senior research associate at the Georgetown University Health Policy Institute. To get started, Bangit suggests statehealthfacts.org, a site run by the nonprofit Henry J. Kaiser Family Foundation. It provides information about consumer protection, plan features required by each state, and links to government-run informational sites.

WHAT TO AVOID

Push insurers for a copy of the "Explanation of Benefits" (EOB), which is more detailed than the standard summary, Bangit says. "They'll say you can't have it until you sign up, but you need it to do your research, so insist on reviewing it," she says. Bangit recommends avoiding plans with an annual benefit cap. Lifetime benefit maximums of $1.5 million to $2 million are more common and less alarming, she says.

Comparing plans can be tricky for those with chronic conditions or in need of special care. Insurers aren't necessarily willing to say how much they'll reimburse for a procedure. Even when plans have a maximum out-of-pocket level, some drugs or procedures may be left out. State laws vary on whether insurers can exclude coverage because of preexisting conditions.

Non-employer-based group plans, known as association plans, may also be available. For example, the New York-based Freelancers Union offers a plan for members. To qualify, an individual must show he has freelanced for at least 20 paid hours in the previous eight weeks or earned $10,000 over the prior six months.

Scrutinize these kinds of offerings. Problems have arisen from confusion over plans that were really limited-benefit plans, not full-blown insurance coverage. The plans, often pitched on TV, partially mirror typical policies by charging a monthly fee and by having discounted prices for doctor visits, prescriptions, or other services. But they generally don't cover expenses such as surgery and hospital stays.

It's not just late-night TV pitchmen who offer confusing limited-coverage plans: Thousands of people bought what they thought was comprehensive insurance from programs licensed through AARP, which got caught up in the debate over limited plans last year.

Senator Charles Grassley (R-Iowa) accused AARP of licensing limited plans from United-Health Group under the misleading names "Essential Plus Health Insurance Plan" and "Essential Health Insurance Plan." Neither covered the huge expenses of those who became seriously ill. AARP suspended marketing the plans and in April said it was discontinuing them. "Ensuring the protection and keeping the trust of our members ... drives all that we do," AARP CEO Barry Rand said then. In the health-insurance market, it's no easy task. BW

ALTERNATIVES TO COBRA

Once the current government subsidy for COBRA health insurance premiums expires—if it isn't extended—other insurance options may make more sense. Here are some guidelines.

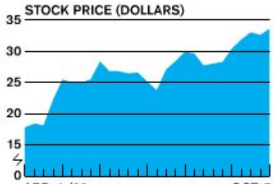
TAKE TIME TO DECIDE	You have 60 days to decide whether to get COBRA. If you might get a new job quickly, there's little harm in waiting. Not all health-related benefits are covered under COBRA or the subsidy program, so review documents carefully.
LOOK TO YOUR STATE	State group plans vary greatly, as do eligibility requirements. Consumer advocates warn that some options, known as limited or fixed indemnity policies, don't offer good value. Start a search at statehealthfacts.org.
VET ASSOCIATION PLANS	Non-employer-based group plans, known as association plans, may be available. Problems have arisen from confusion over plans that were really limited-benefit plans, not full-blown health insurance coverage.
EXPLORE INDIVIDUAL PLANS	Healthy people can likely find a good individual policy at substantially lower cost than a COBRA plan, says Jon Moss, of Moss Benefits Group. Ask the plan provider for the detailed "Explanation of Benefits" document.



COACH'S WINNING BAG OF TRICKS

Coach (COH), one of the few luxury-goods companies that quickly revised its strategy last year to avoid getting knocked out by the recession, was in solid shape by the end of its fiscal year on Jun. 30. That has fired up its stock, which rocketed to 33.44 a share from 11.41 in early March. The company "reacted quickly and prudently" by cutting price levels without sacrificing product value and its 70%-72% gross margins, says Jennifer Milan of investment firm Sterne, Agee & Leach. A designer and maker of upscale products for women and men, Coach is a leader in handbags, which account for 62% of total sales. "Coach has significant growth opportunities," Milan notes, in both domestic and foreign markets, particularly in China. She rates Coach outperform with a 12-month target of 38.

PROFITABLE POCKETBOOKS



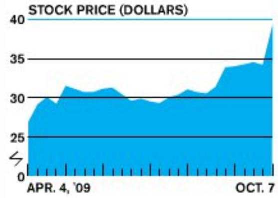
Data: Bloomberg

Michelle Clark of Morgan Stanley (it did banking for Coach) rates the retailer overweight. She says the company's strategy of reducing the average handbag price from $325 each to $285 is working. She has upped her fiscal 2010 earnings forecast to $2.01 a share from $1.84, and her 2011 estimate to $2.28 from $1.98. Even with the stock's huge advance, Coach is still attractive because the current price "fails to account for normalized earnings above $2 a share and for operating margins above 31%," says Clark.

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NOTHING TO SNEEZE AT



Data: Bloomberg

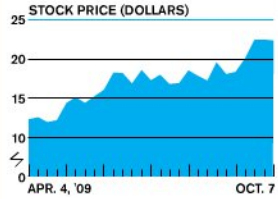
Walgreen: The Flu Season Factor

Some pros are snapping up shares of Walgreen (WAG) as a play on the flu season.

Shares of the largest U.S. retail drugstore chain in revenue terms have climbed to 39.12 from 21 a year ago, in part because of solid fiscal fourth-quarter (ended Aug. 31) results that beat the Street's estimates. That plus the flu season ahead should push up Walgreen's shares, says Robert Willoughby of Bank of America Merrill Lynch, who rates the 6,500-store chain a buy. "A more severe flu season implies some upside to our revenue and earnings forecasts," he says. Already demand this year for products such as flu shots and cold medicines is stronger than in 2008.

Derek Leckow of Barrington Research rates Walgreen outperform with a 12-month target of 60, based on his earnings estimate of $2.28 a share for fiscal 2010 and $2.88 for fiscal 2011.

IN DEMAND EVEN IN A HIRING SLUMP



Data: Bloomberg

Recruitment Riches for Taleo

You might expect the recession to clobber a company like Taleo (TLEO), which provides corporations with a software system to recruit, assess, and improve their workforce. But Taleo's stock has zoomed to 22.39 a share from 5.37 on Nov. 21, 2008, a 52-week low. Business at Taleo "remains robust," says Brad Reback of Oppenheimer, who rates the stock outperform. Taleo, he says, "can generate double-digit earnings and free cash flow growth over the next few years."

Taleo Chairman and CEO Michael Gregoire says that despite massive layoffs, corporate giants, including Citigroup, Intel, and JPMorgan Chase (all Taleo clients), continue to fill key positions, and that's when they need Taleo's services.

Tom Ernst Jr. of Deutsche Bank sees Taleo earning 21¢ a share in 2010, vs. a loss in 2009. He rates Taleo a buy with a one-year target of 27. |BW|

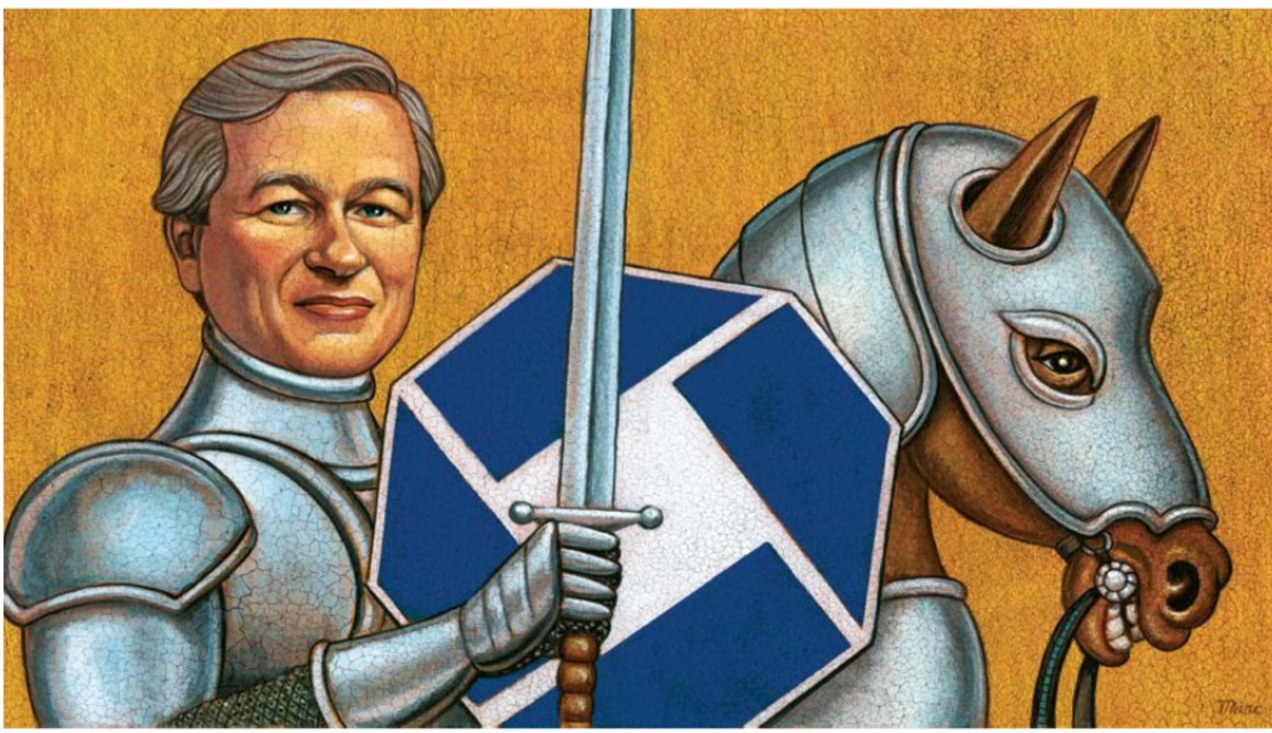
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BOOKS | MARA DER HOVANESIAN

Jamie Dimon: Lucky or Good?

How the JPMorgan Chase CEO weathered the global financial maelstrom and emerged almost unscathed



MARC BURCKHARDT

Few figures of today's financial world are more respected than Jamie Dimon, CEO of JPMorgan Chase. For a banker to emerge from the financial meltdown with mere flesh wounds might be accomplishment enough. But for Dimon—whose rise, fall, and rise again has been one of the most compelling stories on Wall Street for decades—the crisis proved he is much more than a survivor. Dimon has earned the ear of the U.S. President, the gratitude of the Treasury Dept. for helping the U.S. escape financial ruin, and the respect of legendary investor Warren Buffett.

Dimon's colorful career, from ousted Citigroup heir apparent to top dog of U.S. banking, is deftly chronicled in *Last Man Standing: The Ascent of Jamie Dimon and JPMorgan Chase* by Duff McDonald, a contributing editor at *New York* magazine. The book is one of the more intimate portraits of the 53-year-old banker, supported by interviews with Dimon, his family, and trusted lieutenants.

One potential irritation: McDonald recounts events in chronological order, meaning readers must wade through several chapters of ancient history before they get to the drama suggested by the book's title. This is a bit frustrating since plenty of controversy still swirls around Dimon's actions of the past 18 months: Did his financial moves force Lehman Brothers into bankruptcy? Did his angling to

take over Bear Stearns represent ruthless opportunism? No on both counts, McDonald concludes. He ultimately describes back-room conversations that show Dimon coming close to easing away from the Bear Stearns deal altogether. These never-before-reported talks reveal Dimon's skillful hand in negotiations with regulators and CEOs of the troubled investment banks at the epicenter of the crisis.

A blow-by-blow account of events provides valuable insight into "Dimonology." The JPMorgan Chase CEO sent hundreds of workers into Bear Stearns to get a clear picture of that company's woes, and he demanded updates from them every three hours. He kept his board apprised with a similar frequency. At one point, his closest confidants began to balk at the deal. But, demonstrating the detachment of a master negotiator, Dimon prevailed. "I have never seen him make a decision based on emotion," Buffett observed to McDonald.

Warren Buffett says of Jamie Dimon: "I have never seen him make a decision based on emotion"

In its lengthy lead-up to recent events, *Last Man Standing* provides rare tidbits about Dimon's school years and upper-middle-class upbringing mainly in New York City. From early on, Dimon showed his ambition, which sometimes took the form of an attitude problem, according to his primary school teachers. He also demonstrated an "early capacity for ethical leadership," writes McDonald: After the only African American in his all-boys prep school was expelled from class for acting out, the teacher commented that "600,000 died to free the slaves, and this is the gratitude we get." Dimon stormed out of the room in protest.



Last Man Standing: The Ascent of Jamie Dimon and JPMorgan Chase **by Duff McDonald; Simon & Schuster; 340pp.; $28**

The executive's well-known penchant for "sweating the details" comes through clearly, as does his ferocious ego. In the 1990s at Commercial Credit—a predecessor to Citigroup—a youthful Dimon earned a reputation as an impetuous "hothead." He once approached a whiteboard in a conference room during a meeting, erased all the names listed under a manager he considered "an obstacle," and rewrote the names under his own. His nemesis soon resigned.

As McDonald acknowledges, *Last Man Standing* covers some of the same ground as another work on Citigroup and its CEO, Sandy Weill, *Tearing Down the Walls* by *Wall Street Journal* writer Monica Langley. Like the previous work, McDonald's book shows that both Weill and Dimon were equally "early and enthusiastic participants" in the move to create giant money center banks. That means Dimon must share some of the blame for creating what the author terms a "disaster waiting to happen."

McDonald also makes clear that JPMorgan Chase's position of strength wasn't entirely the result of Dimon's leadership. Bill Winters (who was edged out of the bank in a succession of maneuvers on Sept. 29) was clearly the strategist who advised the bank to shed an $8 billion structured investment vehicle that decimated Citigroup's capital reserves. McDonald also shows that although Dimon fared better than rivals, he miscalculated the severity of the crisis in its early days.

McDonald got sufficiently inside Dimon's head to know his thinking on succession planning. In the last few pages of the book, the author speculates that Jes Staley, former head of the asset management group, will be Dimon's successor. Dimon has no plans to retire soon, but Staley's recent rise to head of the investment bank (edging out Winters) is a signal he's being groomed for the top spot. Once there, Staley may find that there are big shoes to fill. |BW|

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The Low-Ball Bid for Bear

BEAR STEARNS

How did JPMorgan Chase arrive at its low, $2-per-share offer for Bear Stearns in a whirlwind deal in 2008? "I tell people buying a house and buying a house on fire are two different things," explained CEO Jamie Dimon during an interview that year on *Charlie Rose*. It wasn't really a question of value but of "how much risk can we bear."

To view the video, go to **bx.businessweek.com/jpmorgan-chase/reference/**

TECH & YOU | STEPHEN H. WILDSTROM



Call It Windows Immobile

Microsoft's upgraded software doesn't even come close to challenging the iPhone

The last time Microsoft delivered a major upgrade to its smartphone software, Windows Mobile 6, in early 2007, Apple's iPhone was still five months out on the horizon. You can tell how radically Apple changed expectations about smartphones if you pick up any Windows Mobile handset today. The software seems positively quaint.

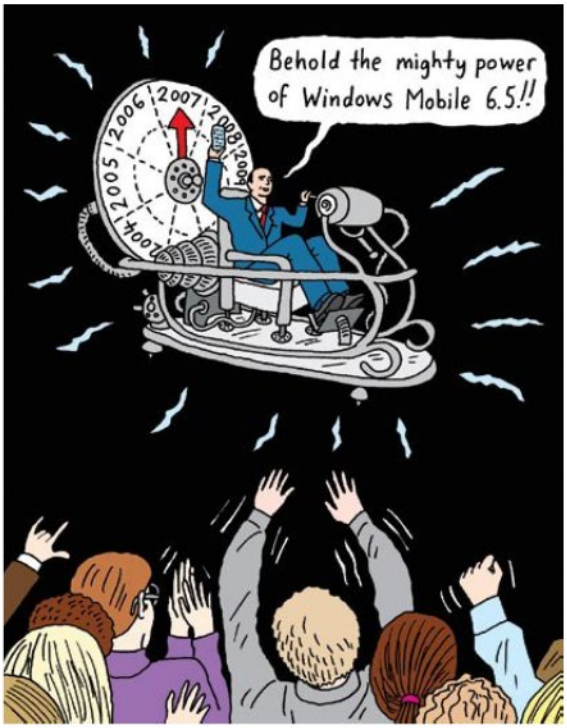
On Oct. 6, Microsoft released a significant upgrade, Windows Mobile 6.5, on HTC handsets from AT&T and Verizon Wireless. Unfortunately the results fall far short of what Microsoft requires to get back into the top tier of mobile communications. And it won't get another shot until version 7.0, a complete overhaul that should appear in late 2010.

Windows Mobile 6.5 sports a new screen design that eliminates just about all vestiges of the Windows desktop interface. In its place is a home screen inspired by Microsoft's latest Zune media player and an iPhone-like grid of applications.

These changes help, but they don't go far enough. The biggest problem with the design is that it has to work on a broad range of handsets. There are WinMo phones with touchscreens and physical keyboards, such as the European version of the HTC Touch pro2, which I used to test the software. There are also handsets with keyboards and no touchscreens, and those with touchscreens and no keyboards.

It's hard to see how any single interface would be a match for all these combinations. In the case of WinMo, all kinds of things go wrong. If, for example, you have an e-mail message or Web page that doesn't fit on a single screen, you flick your finger to move the text up, just as you would expect. But the display also has scroll bars for use with a stylus. This wastes screen real estate and causes confusion, because sliding the scroll bar up actually moves the text down.

Also, Microsoft supports only the relatively insensitive "resistive" touchscreens, not the finger-friendly "capacitive" screens used by phones running Google's Android software, as well as the Palm Pre and the iPhone. (Microsoft plans to rejigger version 6.5 within a few months so it can handle capacitive screens.)



On the positive side, the new version of Internet Explorer on these handsets is much better than its predecessor—even if it is still a step down from browsers on iPhone and Android handsets. One helpful feature is a slider at one edge of the screen that lets you expand or shrink text and images. But it doesn't work consistently. You cannot, for example, use it to rescale Bing Maps, Microsoft's alternative to Google Maps.

Microsoft is taking a couple of steps to make Windows Mobile feel more up-to-date. My Phone is an online service that backs up your phone content and gives you Web access to contact and calendar information. It is more limited than Apple's MobileMe, but unlike that $99-a-year service, it is free.

Microsoft also is launching a store called Marketplace that will bring thousands of Windows Mobile apps under one virtual roof. Each wireless company will get a section of the Marketplace for sale of carrier-specific apps. These will be included on phone bills, and the carrier will get a cut; others will be charged to a credit card, with revenues split 70-30 between the developer and Microsoft.

Microsoft executives concede that version 6.5 is a placeholder until a more modern Windows Mobile 7 is ready. The company plans to impose much stricter rules for hardware, which will allow a more coherent software design and a better user experience. WinMo 6.5 will plod along until then, but Microsoft and its software are sure to take a lot of abuse. |BW|

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PHOTOGRAPH BY BRAD TRENT; ILLUSTRATION BY PETER ARKLE

070 FEEDBACK

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THE STOCK MARKET
A NEW GAME?

What, exactly, is "normal" when it comes to assessing the Great Recession's stock market and economy? The diversity of opinions was the subject of "Searching For True North" (Cover Story, Oct. 5), a debate that spilled over to the responses we got. Readers argued for and against the view that a low-growth, low-return world is the "new normal"—with one commenter suggesting that any idea of normal, new or old, is bogus. –*Roben Farzad*

Both market theories—the "new normal" and the "massive reversion to historical patterns"–could be right in the long run. From 1900 through 1984 there were three long stretches (15 to 18 years each) where conventional wisdom was that the secular bull markets were dead. Each was eventually followed by a strong upswing in stock prices. The current "long stretch" of dismal returns seems to be another one of those periods.

Robert J. Parish
JUPITER, FLA.

There's another view of "normal" that has come out of the crisis stronger than ever: that "normal" doesn't exist at all, that the belief in market equilibrium is part of the kit bag of ideas—including the efficient market and rational expectations—that have been effectively undermined.

Posted on TheDeal.com by Editor in Chief Robert Teitelman



The article says "the sacred texts of investing need to be rewritten." But a careful study of *Security Analysis* or *The Intelligent Investor* (both by Benjamin Graham, the father of value investing) will help inoculate the student against the nonsense that gets passed off as investment wisdom.

Matt Nellans
FORT MYERS, FLA.

INVESTING
WHY RUSSIA'S PROMISE MAY BE ILLUSORY

"The Peril and Promise of Investing in Russia" (In Depth, Oct. 5) gives a misleading impression of the nation's "140 million voracious consumers." Russia's population is aging relatively rapidly, poverty is high, and the middle class is small. Figures for disposable household income are skewed by a small group of very wealthy Russians.

James Thomassen
AUSTIN, TEX.

COMPANIES
DOWNSIZED DOESN'T NECESSARILY MEAN LEAN

Regarding "Business is Lean, Fit, and Ready to Grow" (Business Outlook, Oct. 5): Company headcounts, payrolls, and budgets may be smaller than they were in previous years. But little does not mean lean. Lean means having less waste and more muscle.

Tom Pryor
PANTEGO, TEX.

MARKETING
A BROADER MEASUREMENT OF THE BEST BRANDS

Why did you use only sales and earnings to choose the "100 Best Global Brands" (Special Report, Sept. 28)? Why not also consider a corporation's adverse impacts on the environment, humans, and animals?

Margaret Hurley
ROCHESTER, N.Y.

LABOR
ANDY STERN'S CONCERNS: WHAT ABOUT TAXES?

Regarding "Union Leader Andy Stern on the Future of Big Labor" (FaceTime, Sept. 28): What a caring guy the SEIU's Andrew Stern is to be concerned about the health aide who lost her family ranch because of medical bills. Apparently he doesn't have the same compassion for those who've lost the family farm because of out-of-control property and estate taxes. Where is his voice on this issue?

Debra Beetem LaRoche
PHOENIX

CORRECTIONS & CLARIFICATIONS

A chart that accompanied "Finally, a Big Green Apple?" (What's Next, Oct. 5) gave the wrong percentages for Apple's estimates of its carbon emissions. The correct breakdown is: 53% from product use, 38% from manufacturing, 5% from transportation, 3% from facilities, and 1% from recycling.

A stock market timeline accompanying "Searching For True North" (Cover Story, Oct. 5) erroneously said President Nixon was impeached in 1974. He resigned as President that year.

COMPANY INDEX

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An IMF Just for Emerging Markets

Developing countries don't trust the fund to serve their interests. Solution: An EMF

Fresh from its annual meeting in Istanbul on Oct. 6-7, the International Monetary Fund is taking a moment to celebrate itself. The IMF rediscovered its role as a lender of last resort in the global crisis (with Iceland a notable rescue). Earlier this year it got an extra $500 billion from member countries to triple its lending capacity. And it is positioned to manage the G-20's much-hyped peer review of countries' monetary, fiscal, and financial policies.

But below the surface, problems are intensifying: The IMF's ability to stabilize the global economy may hit a wall because of resentment among emerging economies. Developing nations have long complained about the extent to which the U.S. and Western Europe dominate the 186-member group—and about the austerity the fund traditionally imposes on borrowers.



Increasingly, many of these nations are reluctant to borrow from the fund. Instead, they run current account surpluses—exporting more than they import and holding the extra proceeds as foreign exchange reserves. Forex reserves are now more than 15% of global gross domestic product, up from less than 5% in 1993—with emerging economies counting for most of the change. Hanging on to this cash depresses global trade and makes it harder to sustain a recovery. (It also lowers U.S. export levels.)

The solution? Developing nations should form an Emerging Monetary Fund, or EMF.

The structure of the IMF made sense when it was set up after World War II. The U.S. (the main creditor) and European nations (the likely borrowers) were the major countries of the capitalist world, with voting rights balanced between the two. Over the next 50 years, colonies gained independence, communism fell apart, and—most important—some fast-growing East Asian economies became part of world financial markets. But the IMF is still dominated by the U.S. and Europe.

By the early 1980s this was irksome to the developing world, leading to accusations that the IMF helped banks over borrowers in the Latin American debt crisis (in the case of Bolivia, for example). It became more than irksome in the Asian financial crisis of the late 1990s, when the IMF backed deeply unpopular policies, including severe fiscal austerity for South Korea, Thailand, and Indonesia. And last year anger surfaced over the hands-off approach to problems in the U.S. and Europe. Argentina's IMF board representative, Hector Torres, argued publicly that the IMF failed to spot the subprime crisis because it doesn't hold the U.S. to the standards it applies to emerging markets.

To be effective, an international lending organization must be trusted by potential borrowers. If a fire breaks out in your house you want the firefighters to put it out as soon as possible, not insist you clean the basement first. And you don't want the firehouse to be run by a group with a self-serving agenda.

An Emerging Monetary Fund—an idea supported by such experts as Arvind Subramanian, a senior fellow at the Peterson Institute for International Economics—wouldn't have the U.S. and Western Europe at the table. But it would have little trouble funding itself. Brazil has more than $200 billion in hard currency reserves. Russia has some $400 billion; China an eye-popping $2 trillion.

As for loan policy, at first the group could copy the design of the Flexible Credit Line, a new IMF loan with few strings attached. So far the loan has only three takers—Poland, Mexico, and Colombia—because other eligible countries, particularly in Asia, are still wary of the fund. An EMF version would likely draw dozens of customers and immediately play a stabilizing role.

Since an EMF would be open to all countries in Latin America, Africa, and Asia, it could easily reach 100 members. And it could work with the IMF, which could specialize in very difficult cases. The EMF would be your friendly neighborhood physician or pharmacy; the IMF could run intensive care.

An EMF would create a much needed buffer in a world of turbulent capital flows. And the U.S., which sees big trade surpluses in China and other nations as destabilizing, would benefit. Until emerging nations have a lender they feel they can rely on, they'll continue to build currency reserves. They need a fund they can trust. |BW|

Simon Johnson, a professor at the MIT Sloan School of Management and a senior fellow at the Peterson Institute for International Economics, was the IMF's chief economist from March 2007 to August 2008.

Jack and Suzy Welch are off while Jack recovers from a back infection.

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